

**Report of**

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**“An East Asian Community”  
and  
New Dynamism of Regional Governance**

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**The 2nd Year**

**2005 October – 2006 September**

**Supported by  
The Japan Foundation Center for Global Partnership (CGP)**

**The Council on East Asian Community (CEAC)**

## Preface

As discussions both within and beyond Japan regarding the regional integration of East Asia have accelerated in recent years, the Council on East Asian Community (CEAC) launched a 3-year project on “‘An East Asian Community’ and New Dynamism of Regional Governance” (October 2004–September 2007) supported by the Japan Foundation Center for Global Partnership (CGP). The project aims to clarify the root, background, and theoretical framework of the concept of an East Asian Community and to provide a policy perspective regarding how the United States should partake in this framework taking intents and strategies of Asian countries into consideration.

In its 1<sup>st</sup> year (October 2004–September 2005), CEAC held the 1<sup>st</sup> International Workshop on “An East Asian Community and the United States” on June 17-19, 2005 in Tokyo, with the participation of Mr. Ralph COSSA, President of the Pacific Forum CSIS and representatives from five think tanks from China, South Korea, Indonesia, Singapore, and Thailand. In the 2<sup>nd</sup> year (October 2005–September 2006), CEAC held the 2<sup>nd</sup> International Workshop on June 20-21, 2006 in Tokyo, with the participation of representatives of think tanks from Indonesia, South Korea, Malaysia, Singapore, Thailand, and the United States. Following the International Workshop, on June 22, the “Japan-US-Asia Dialogue” was held with the co-sponsorship of the Global Forum of Japan (GFJ) and the Pacific Forum CSIS. 78 participants, composed of intellectuals, economists, and politicians from Japan and other countries including CEAC members, attended the Dialogue. In the 3<sup>rd</sup> year of the project, CEAC will publish a book in English on an East Asian Community and its relationship with the United States as an accomplishment of the 3-year project.

This report consists of 7 parts, which are based on papers prepared for the 2<sup>nd</sup> International Workshop, in addition to the Workshop materials such as the program and the participants list. The 7 papers written by the Workshop participants from Japan, Singapore and the United States are the preliminary drafts of a book to be published in the 3<sup>rd</sup> year of our project. The report is posted on the website ([www.ceac.jp](http://www.ceac.jp)) of CEAC to report the result of our 2<sup>nd</sup> year’s activities to the general public of Japan and abroad.

Upon publishing this report, I would like to extend my appreciation to CGP for their support throughout this project.

September 30, 2006

ITO Kenichi  
President  
The Council on East Asian Community  
(CEAC)

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# 1. Emerging East Asian Community? - Political Process

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## Introduction

Regionalism and Regionalization in East Asia and wider Asia-Pacific region have accumulated as multi-layered frameworks of Mega-regionalism, sub-regionalism and various forms of Ad-hoc multilateralism<sup>1</sup>. Among various types of regional framework, the recent trend represents the rise of “East Asia” especially since 1997, the year launching of the ASEAN+3 Summit Meeting. Although it is relatively a new trend to forge regional cooperation based on the ASEAN+3 processes, there have already been 48 official Meetings among 17 areas (e.g. finance, trade and investment, labour, health, IT, tourism, education, etc.) come into force under the framework of 10+3 process<sup>2</sup>. Based on such accumulative regionalization process, the East Asian Summit (EAS) launched since December 2005 represents the significant milestone of community building in East Asia.

Although the term “East Asia” has been given a birth as the political process, its signified image (*signifier*) as a region has been varied by observers. One of the most important fundamentals of East Asia has been the *de facto* **regionalization** represented by the drastic expansion of intra-regional exchanges and increased interdependence among countries in the region, particularly after the late 1990’s.

During the last 10 years, the trade volumes between Japan and China, China and South Korea, and China and ASEAN have increased by four, eight and six fold respectively. In the figure of 2003, the East Asian intra-regional trade share has marked 53.3% (including Taiwan and Hong Kong) while it was only 33.6% in 1980. The figure exceeded the rate of NAFTA (44.5%) and getting closer to the rate of EU (60.3%). Its share of the global GDP accounts for one fifth, and countries in the region now hold about a half of the world foreign reserves. Moreover, with the increased trends of horizontal production networks in the manufacturing sectors, East Asia has provided the cross-border ‘integrated economic space’ to forge dynamic competitiveness.

The **functional regionalization** in East Asia has facilitated by a growing awareness of enormous potential and opportunities of closer regional cooperation on common interests and concerns. It is noteworthy that several major incidents after the late 1990s played a role as a vital catalyst for foundation of various ASEAN+3 processes. One is the financial crisis in 1997, which awakened people of the region to the need of a regional approach to secure their financial institutions and financial markets. The other is the rise of asymmetrical threats such represented by the terrorist attacks on September 11<sup>th</sup> 2001, which underscored the importance of regional cooperation in addressing terrorism and other transnational issues.

In dealing with these events, regional networks of functional cooperation have spread swiftly in wide-ranging issues, such as finance (the Chiang Mai Initiative and the Asian Bond Market Initiative), various types of Free Trade Agreements, and transnational issues (terrorism, illicit drug trafficking, sea piracy, trafficking in persons, non-proliferation and public health), etc. Although functional cooperation does not automatically define the fixed membership in nature, ASEAN+3 formats has provided a common divisor as a regularized official process to cover these functional agendas.

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<sup>1</sup> T.J. Pempel, *Remapping East Asia: The Construction of a Region* (Cornell University Press, 2005)

<sup>2</sup> ASEAN Secretariat, “ASEAN Plus Three Cooperation” <http://www.aseansec.org/16580.htm>

Finally, the **regionalization in East Asia as a community building** is more comprehensive process. The term ‘community’ is again a multifaceted concept of which many observers have different images<sup>3</sup>. Most broad sense of community could be defined as a group of countries sharing some values in common (shared values), having a sense of giving oneself to another (attribution), and interacting beyond functional bases (comprehensiveness). If those dimensions are applied, the record of building bloc process of ASEAN+3 and East Asian Summit could be characterized as a process of community building<sup>4</sup>. The “Joint Statement on East Asian Cooperation” agreed at the third ASEAN+3 Summit in November 1999 outlined the member countries’ commitment to economic, social and political areas of cooperation and called for each Ministerial process to engage in the process. The Kuala Lumpur Declaration at the First East Asian Summit in December 2005 has also identified the process of “dialogue on broad strategic, political and economic issues of common interest and concern with the aim of promoting peace, stability and economic prosperity in East Asia”.

This paper tries to focus on opportunities and obstacles for the East Asian Community by especially focusing on the political process of ASEAN+3 and East Asian Summit. First, the paper underscores the framework of analysis, which aims to provide the current trends of creating a ‘region’. Second, the paper analyses the process of the ASEAN+3 and East Asian Summit to extract the commonality and diversity of the concept of “East Asia”. Finally, the paper outlines the current ad-hoc cooperation mechanism and its possibility to apply in context of new regionalism.

## **Framework of Analysis: Nature of “Post”- Mega Regionalism**

### ***First Wave of Regionalism: Failure in 1960s***

The term ‘region’ could be defined in various terms. In international relations, it generally indicates the multilateral groupings of neighboring nations. However, when it comes to the term ‘regionalism’, it rather suggests a functional relation that bundles multiple nations with their political, economic and cultural inheritance, often based on the advantages geographical proximity<sup>5</sup>. If one tries to look into the ‘regionalism’ we need realize that it is the dynamic concept of geopolitics/economics, which rests between the global governance and the bilateral rational choice of the government. Thus, ‘Regions’ are fluid and complex mixtures of physical, psychological, and behavioral traits that are continually in the process of being re-created and redefined<sup>6</sup>.

Historically, after the WWII, it is often said that there have been three waves of regionalism<sup>7</sup>. The first wave arose in 1960s, among the members in West Africa, Latin America and Caribbean States etc. These regionalisms took form as Free Trade Area, Customers Union and other trade agreements with taking advantage of the special treatment in the GATT Article 24<sup>th</sup>.

It is to our common knowledge that these first waves of regionalism ended in failure (except for the

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<sup>3</sup> This confusion might further deepen by how the concept is introduced (or translated) in local languages. For example, the term *kyodotai* (共同体) in Japanese indicates high degree of adhesion within the group bundled by consanguinity and ownership, which is more determined concept than the casual ‘group of people sharing (something) in common’.

<sup>4</sup> In this regard, areas of cooperation of which ASEAN+3 and East Asian Summit cover are more comprehensively defined than APEC (economic oriented) and ARF (political-security oriented) process.

<sup>5</sup> Robert Z. Lawrence, *Regionalism, Multilateralism, and Deeper Integration* (Washington DC: The Brooking Institution, 1996).

<sup>6</sup> T.J. Pempel, *Remapping East Asia*, p.4; Edward D. Mansfield and Helen V. Milner, eds., *The Political Economy of Regionalism* (New York: Columbia University Press, 1997).

<sup>7</sup> Jaime De Melo and Arvind Panagariya eds., *New Dimensions in Regional Integration* (Cambridge University Press, 1993).

original European Community and EFTA) because of various reasons. 1) There were no participation of big economies to these regional gathering, 2) these regions tended to pursue the import substitution policy, and 3) they rather emphasized the protection of national industry sectors through preferential trade agreement and strong protectionist policy. Some lessons learned from the failure of the first wave was that the region pursuing the import substitution among small and medium size economy will lose their competitiveness and decrease its validity, especially the international economy became more interdependent in 1970s<sup>8</sup>.

### ***The Second Wave in 1980s: Premise of ‘Open Regionalism’***

The Second Wave, derived from the famous term by Prof. Jagdish Bhagwati, came along in late 1970s and 80s with the rising of wider regionalism or ‘mega-regionalism’ based on the principle of the ‘open regionalism’<sup>9</sup>. Rising East Asian economy and the decline of the dominant economic status of the United States (“After Hegemony”: Robert Keohane) had both promoted the relative rise of regional groupings such as the Asia Pacific Economic Cooperation (APEC) and Asia Europe Meeting (ASEM) process.

The concept of open regionalism has also been applied to the political and security cooperation in the Asia Pacific. Based on the strategic environment after the end of Cold War in Asia, nearly 20 countries in Asia-Pacific have agreed to form the ASEAN Regional Forum (ARF) in 1994 to promote confidence building among nations by increasing exchanges among officials/non-officials contacts and transparency of their security policies.

The premise of the open regionalism was based on ‘inclusiveness’ and ‘equality’, where countries in the region are, in principle, open to participate in the forum. The membership of the regime is based on the existence in the region, not exclusively by its characteristics. “Engagement” was the core principle for this type of multilateral cooperation by the inclusion of the states, as the APEC engaged Taiwan and Hong Kong, and ARF successfully engaged China, Russia, enlarged ASEAN, India, Pakistan and North Korea.

### ***The Third Wave: Rise of Bilateralism/Ad-hoc Mechanism to form Region***

As we entered in the 21<sup>st</sup> century, we have now witnessed the new forms of regionalism in Asia, which does not necessarily adhere to this unequivocal inclusive nature. The emerging impetus of bilateralism and functionalism—such as bilateral Free Trade Agreements (FTAs) and other functional cooperation—are made up by the capability and the willingness of actors. Although most of the existing coalitions have the principles of open memberships and do not exclude the future participation of non-member, the tacit assumption of such coalitions of the willing does not necessary includes the countries that are reluctant to cooperate within the framework. It virtually leads to the politics of exclusion.

The primary benefit of such coalition of the willing may be; they could evolve cooperation with like-minded states to ensure higher level of cooperation. It could even be regarded as a counter argument toward ‘inclusive region-based’ cooperation like the APEC and the ARF, which recently failed to address vigorous developments for cooperation as long as participating countries “continue to move at a pace comfortable to all participants and on the basis of consensus.” Instead, the coalition of the willing will set up the higher degrees of cooperation without the interference of external actors, and invite them after the coalition has set up the agenda.

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<sup>8</sup> Also, these LDCs pursued attempting such unions sought to allocate industries by bureaucratic negotiation and to tie trade to such allocations, rather than use trade liberalization and hence prices to guide industry allocation. *Ibid*, p.28.

<sup>9</sup> Jagdish Bhagwati, “Regionalism and Multilateralism: an overview” in Jaime De Melo and Arvind Panagariya eds., *New Dimensions in Regional Integration*, op.cit.

This paper tries to argue that the current process of ASEAN+3 is more likely to be based on the networks of such bilateral frameworks and agreements. Financial Cooperation such as Chiang Mai initiative is the bundle of bilateral swap arrangements; other functional cooperation is also being made through coalitions of the willing.

## **Development of ASEAN +3 Framework**

### ***Financial Cooperation***

The ASEAN+3 process has been developed by the efforts to recover from the Asian currency crisis. Even today, the most advanced area of cooperation within ASEAN+3 is in the field of financial cooperation.

Before having the idea of Chiang Mai Initiative, Japan's initial proposal to create a \$100 billion Asian Monetary Fund (AMF) was aborted due to opposition from the United States and the IMF. Also, China was said to be reluctant to go with the idea. The overall sentiment, however, has changed substantially in 1998 as a turning point. After witnessing currency crises in Russia and Central America, the U.S. has come round to thinking that it would be more positive to let Japan play a greater role in financial cooperation in Asia. China has also realized that the stabilization of the global economy, particularly that of the Asian economy, is crucial to its own economic development, and thus has come to support the idea of creating a region-wide framework for currency stabilization<sup>10</sup>.

As a major step in this direction, the Chiang Mai Initiative, a network of bilateral currency swap agreements, was launched in 2000. The Chiang Mai Initiative is also meaningful as a confidence-building step. It has introduced a crisis prevention mechanism and sent out a message that Asian countries would join forces in the event of crisis. Such signaling is quite important because it discourages to some extent speculative moves by foreign funds and provides some assurance that a crisis would subside at an early stage even if one occurred.

Beyond the Chiang Mai Initiative, ASEAN+3 is currently seeking for establishment of Asian Bond Market, to fund especially to Small and Medium Enterprises in East Asia to subsidize the mid and long-term capital resources. In addition to the Bond Market Initiative, there are several ideas are floated to stabilize regional financial and equity market. Some argues that East Asian countries could shift from the current de facto dollar peg system to a band, basket and crawling (BBC) regime with each country pegging its currency to a different currency basket. For instance, South Korea, which competes with Japan in exports, should adopt a basket in which the yen carries substantial weight. The trade volume between the two countries may not affect rather than their concern on competitiveness in the global market, that is, in exports to the U.S. and Europe.

Newly Industrializing Economies (NIEs) are generally in the same situation. They should peg their currencies more closely to the yen rather than to the dollar so as to avoid negative impacts from the volatility of dollar-yen exchange rates. But the yen could dominate a much smaller portion of the currency basket for China and other countries that are far behind Japan in economic development and do not compete with Japan in exports. They can change the composition of their currency baskets according to changes in their respective trade structures. When countries come to have similar trade structures, the precondition for forming an optimum currency area, they can move into the second stage, which would be to peg their currencies to a single, common currency basket.

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<sup>10</sup> Phillip Y. Lipsy, "Japan's Asian Monetary Fund Proposal" *Stanford Journal of East Asian Affairs*, Vol.3, No.1 (Spring 2003).

### **Functional Cooperation**

On the functional cooperation, there are wide array of cooperation in progress including trade and investment, IT, transnational issues, development assistance, energy security, environmental preservation, disaster prevention, food security and health care. As mentioned earlier, there are 48 consultative bodies covering 17 areas exist within the ASEAN+3 frameworks in progress. What is important here is that the scope of participating countries in such cooperation is decided flexibly and openly according to the characteristics of each area. Countries outside the ASEAN+3 frameworks such as Australia, New Zealand, India and the United States play important role in the functional cooperation.

Functional approach compared to the institutional approach attempts to create a various types of community through the promotion of cooperation in individual fields, rather than building comprehensive institutional and legal frameworks from the outset. Such functional approach is more likely to promote cooperation in East Asia since East Asia has enormous diversity and disparities which makes such approach much more appropriate.

The challenge we face today is how to converge one functional cooperation with another. If we promote various types of FTAs (from Economic Partnership Agreement to Early Harvest-type FTA) without any coordination, the nest of FTAs contains different types of standards which make the 'Spaghetti Bowl' Effect. It is very important to network those bilateral bases of cooperation to regional one, with having high standards of cooperation and harmonization of rules and standards.

Other functional forms were added to the ASEAN+3 framework; the Economic Ministers Meeting was held first in Yangon on 2 May 2000 and has been held annually since then. As Table 1 indicates, other areas such as labor, agriculture, tourism, energy, and environment are also now being discussed at the ministerial level.

**Table 1: Scope of ASEAN+3 Cooperation**

Area	Year of Establishment
Political and Security	2000
Economic, Trade, and Investment	2000
Finance and Monetary	2000
Agriculture, Fishery, Forestry	2001
Labour	2001
Environment	2002
Tourism	2002
Culture and Arts	2003
Energy	2004
Health	2004
Information Technology and Communications	2004
Social Welfare and Development	2004
Transnational Crime and Counter-Terrorism	2004
Science and Technology (SOM only)	2001
Youth (SOM only)	2004

Source: This table is slightly modified from that which is presented in the *ASEAN Annual Report, 2003-2004*, p. 66, <<http://www.aseansec.org/AR05/PR-Partnership.pdf>>.

### ***Political and Security Cooperation***

From the mid-1990s increased support for an East Asian grouping. These included:

- The inauguration of the Asia-Europe Meetings (ASEM) in 1996, which explicitly involved dialogue between Europe and an 'Asian side';
- The traumatic impact on many regional economies of the Asian financial crisis from mid 1997, which prompted many regional states to consider the desirability of greater cooperation to forestall any future crisis and to add greater 'weight' for Asia in relations with international institutions such as the International Monetary Fund;
- APEC's inability to maintain the momentum towards trade liberalisation it had in the mid 1990s;
- A continuing sense that the ongoing development of regional groupings in Europe (the EU) and the Americas (the North American Free Trade Agreement) should be accompanied by greater East Asian cooperation; and
- China's dynamic economic growth which stimulated a rise in the importance of trade among the countries of East Asia.

All these developments contributed to the opening up of 'political space' for an East Asian grouping<sup>11</sup>.

One of the most significant milestones of the ASEAN+3 political processes is the agreement on 'Joint Statement on East Asia Cooperation' at the third ASEAN+3 Summit in November 1999. ASEAN+3 leaders have agreed upon the issue areas of economic cooperation, monetary and financial cooperation, social and human resources development, scientific and technical development, cultural and information areas, development cooperation, political-security area and transnational issues, which should be covered by this process, and mentioned that "political and other fields" are important as follows.<sup>12</sup>

- in the political-security area, they agreed to continuing dialogue, coordination, and cooperation to increase mutual understanding and trust towards forging lasting peace and stability in East Asia;
- in the area of transnational issues, they agreed to strengthen cooperation in addressing common concerns in this area in East Asia.

Another important development in Manila was the informal breakfast attended by the leaders of China, Japan and South Korea. Within the ASEAN+3 gathering, the '+3' component of three-way cooperation was much weaker than the corresponding ASEAN cooperation. In fact, there had never been a summit among the leaders of the three countries in Northeast Asia. At the initiative of Japan's Prime Minister Obuchi, the three leaders agreed to have a separate meeting of their own for the first time.

With the third meeting in Manila, ASEAN+3 clearly established a life of its own as a viable international institution in East Asia. It was determined that its summit would be held annually; it defined the scope of the group's activities as being very comprehensive; it created functional ministerial meetings; and it created an advisory panel to consider future directions. Annual summits, however, have continued to be the focal point for ASEAN+3 cooperation. At the 2000 Singapore summit, a range of new ideas were raised such as the desirability of transforming the ASEAN+3 summit into an East Asian Summit and desirable forms of free trade in the region. President Kim Dae Jung proposed the establishment of an East Asia Study Group (EASG) composed of government officials to 'explore practical ways and means to deepen and expand the existing cooperation' among ASEAN+3; it was tasked to 'assess the recommendations of the EAVG' and to

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<sup>11</sup> Richard Stubbs, 'ASEAN Plus Three: Emerging East Asian Regionalism?', *Asian Survey*, v. 42 no. 3, May - June 2002, pp. 440-455

<sup>12</sup> ASEAN Secretariat, "Joint Statement on East Asian Cooperation" (28 November 1999). <http://www.aseansec.org/5469.htm>

‘explore the idea and implications of an East Asian Summit’.<sup>13</sup>

The EAVG presented its report to the ASEAN+3 summit in November 2001 with the opening statement stating, ‘We, the people of East Asia, aspire to create an East Asian community of peace, prosperity and progress based on the full development of all peoples in the region.’<sup>14</sup> The goals the EAVG agreed upon to create an East Asian community included:

- To prevent conflict and promote peace among the nations of East Asia;
- To promote trade, investment, finance and development in the region;
- To advance human security and well-being, in particular by facilitating regional efforts for environmental protection and good governance;
- To bolster common prosperity by enhancing cooperation in education and human resources development; and
- To foster the identity of an East Asian community by encouraging active exchanges and regular dialogues at both the governmental and non-governmental levels.<sup>15</sup>

The report, based on these goals in mind, made 57 concrete recommendations including 22 major recommendations encompassing five areas of cooperation: economic, financial, political and security, environment and energy, and social, cultural and education. The most noteworthy recommendations included:

- Establishment of the East Asian Free Trade Area (EAFTA) and liberalisation of trade well ahead of the APEC Bogor Goal;
- Establishment of a self-help regional facility for financial cooperation;
- Adoption of a better exchange rate coordination mechanism consistent with both financial stability and economic development.
- Evolution of the annual summit meetings of ASEAN+3 into the East Asian Summit.

The East Asia Study Group examined all EAVG recommendations and presented its report to the 2002 Phnom Penh Summit. This was the first substantive government-level policy agreement reached within the ASEAN+3 process. The EASG report positively assessed the EAVG report by saying: ‘It provided East Asian countries with a good compass to show the right direction towards a bright future of East Asia.’<sup>16</sup> After examining all EAVG recommendations, the EASG concluded that 17 of them should be selected as ‘short-term measures’ to be implemented, and nine of them should be selected as ‘medium-term and long-term measures to require further studies’<sup>17</sup>.

The EASG report was significant in the sense that the newly established framework of ASEAN+3 could agree at all about concrete measures of joint action. However, it revealed its limitations too; the EASG virtually postponed its judgment on difficult issues by designating them as ‘medium-term and long-term measures’. For example, the four recommendations of the EAVG listed above were all categorized as these ‘medium-term and long-term measures’ that required further study. Nonetheless, although limited, the outcomes from the EASG report do show a willingness to move beyond talk into substantive policy actions.

While officials of the EASG deliberated over various measures in 2001 and 2002, the regional political momentum moved from Seoul and Tokyo to Beijing. President Kim Dae Jung’s failure to improve

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<sup>13</sup> *Final Report of the East Asia Study Group, ASEAN+3 Summit*. (Phnom Penh, 4 November 2002), p. 64.

<sup>14</sup> *Towards and East Asian Community: Region of Peace, Prosperity and Progress. East Asian Vision Group Report*, 2001. p. 6.

<sup>15</sup> *Towards and East Asian Community: Region of Peace, Prosperity and Progress*, p. 16.

<sup>16</sup> *Final Report of the East Asia Study Group*, p. 13.

<sup>17</sup> *Final Report of the East Asia Study Group*, p. 13.

the North-South relationship after a historic visit to Pyongyang in 2000 led to declining approval ratings in 2001 and compromised him during the 2002 presidential campaign. A series of leadership changes deprived Japan of opportunities to shape regional policies. Prime Minister Keizo Obuchi, who was a strong supporter of Japan's ties with ASEAN+3, was replaced by Yoshiro Mori after falling ill in April 2000. Mori, unable to improve his popularity, was forced to resign next spring and Junichiro Koizumi took office in April 2001. Koizumi, though immensely popular when he assumed the prime minister, was slow to focus on developing an Asia policy. Rather his immediate task was to improve relations with the United States and to cooperate with the US and the international community after the 9/11 terrorist attacks.

## **Regional Actors and East Asian Community**

### **ASEAN**

In past years, ASEAN strives to become more of a coherent community, through the establishment of the ASEAN Community (articulated in the Bali Concord II in 2003) that constitutes ASEAN Security Community and an ASEAN Economic Community and ASEAN Socio-Cultural Community. These reactions are motivated by how ASEAN try to coordinate two difficult questions: that is to deal within the problems in ASEAN, especially forging trade and investment through FTAs at the same time to deal with the underdeveloped nations namely Cambodia, Laos, Myanmar and Vietnam (CLMV) through the redistribution polity. ASEAN also wanted to lead the process of regionalism in East Asia, by defining its own concept of community building earlier than any other actors in this region in order to maintain their position of “drivers’ seat” in regionalization process.

ASEAN's recent efforts have also shown just how difficult it is to get these nations—some of which have been closely aligned for over 30 years—to think and act as one, especially in the political and security arena. Developing a lowest common denominator for security cooperation among these ten diverse nations is difficult enough. If current established multilateral community-building mechanisms, such as the ASEAN, APT, the ASEAN Regional Forum (ARF) and Asia Pacific Economic Cooperation (APEC) “gathering of economies” are any indication of the willingness of East Asian nations (regardless of how the term is defined) to seriously address issues of regional governance, one should not expect much progress soon.

In building the ASEAN Community, the ASEAN member countries are now committed to developing an ASEAN Charter to provide the constitutional framework for ASEAN. The ASEAN Charter, which will be a landmark constitutional document embodying fundamental principles, goals, objectives and structures of ASEAN cooperation capable of meeting the needs of the ASEAN Community and beyond. It is noteworthy that the Charter aims to promote democracy, democratic institutions, human rights, transparency and good governance<sup>18</sup>. The Charter will include ‘political norms and values’ that would promote transparency and accountability among members.

### **China**

In the meantime, China, which had long been reluctant and passive to any multilateral cooperative frameworks, began to take active initiatives to cultivate its relationship with ASEAN countries. Prime Minister Zhu Rongji, at the ASEAN+China summit in November 2000, proposed to establish an FTA between China and ASEAN countries.<sup>19</sup> In the next year's summit, Zhu agreed with his ASEAN

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<sup>18</sup> Christopher Roberts, “The ASEAN Charter: A Crossroads for the Region?” *IDSS Commentaries*, 1 September 2005. <http://www.ntu.edu.sg/idss/publications/Perspective/IDSS602005.pdf>

<sup>19</sup> Based on this decision, an ASEAN-China Expert Group on Economic Cooperation was created; its report was submitted to the ASEAN+China summit in 2001. See <[http://www.aseansec.org/newdata/asean\\_chi.pdf](http://www.aseansec.org/newdata/asean_chi.pdf)>.

counterparts to conclude an FTA between ASEAN and China within ten years. At the 2002 ASEAN+China summit, China and ASEAN concluded a 'Framework Agreement of Comprehensive Economic Cooperation', which stipulated approaches and modalities to facilitate economic cooperation including an FTA. This agreement included a provision to realize trade liberalization immediately in some sectors, known as the 'Early Harvest program.'<sup>20</sup> In 2003, China became the first dialogue partner of ASEAN to sign its Treaty of Amity and Cooperation. Since then China has continued to expand the scope and depth of its cooperation with ASEAN, with a new bilateral dispute resolution mechanism being agreed upon in 2004 and cooperation in disaster planning and relief operations being undertaken in 2005.<sup>21</sup>

When the idea of an East Asian Community was floated, it becomes more obvious that China was seeking more than just economic benefits through its approaches to ASEAN. By compromising with ASEAN over the South China Sea dispute and China's accession to the TAC—ahead of Japan and other nations—was also an important steps to improve political relations with ASEAN.<sup>22</sup>

## U.S.

The US Secretary of State Condoleezza Rice made a speech on the US's Asia policy on March 19, 2005 at Sophia University in Tokyo. The "Pacific Community" and "openness and choice" were the keywords when she outlined the regional architecture.

The future of *Asia and the Pacific community* will be defined around two great themes—*openness and choice*. Instead of closed societies or economies, instead of spheres of influence, we stand for an open world. Instead of an exclusive club of powers, we stand for a community open to all. But states must choose. They must choose whether to be a part of that community of openness, accepting the responsibilities that go with it. The United States and Japan have already made that choice, and we are honored to have a democratic Japan as a friend.

——Speech by Secretary of State Condoleezza Rice<sup>23</sup>

Prior to that speech, Japan and United States have issued "Joint Statement of the Japan-US Security Consultative Committee" on February 19<sup>th</sup>, with having recognition of welcoming the "development of various form of regional cooperation" while stressing the "importance of open, inclusive and transparent regional mechanisms" as a bilateral common strategic objective in the region<sup>24</sup>. The term "regional cooperation" clearly included the recent strives for developing East Asian frameworks. At the Rice speech, however, such embracement of other regional cooperation was not reiterated, but the "Pacific community" was the only concept when she described the region.

It is still unclear whether the US perceives the East Asian grouping would serve the US regional interests. Several in the US, including ex-Vice Secretary of State Richard Armitage, openly opposed the idea of East Asian community (and holding of East Asian Summit). Apparently three concerns were raised. First, the East Asian community would create or increase the Chinese sphere of influence in the region. Given the growing economy and political influence of China, building of a regional framework without the US might create China-led community, which disturbs the US engagement in East Asia.

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<sup>20</sup> <<http://www.aseansec.org/13196.htm>>.

<sup>21</sup> Source: ASEAN-People's Republic of China, <<http://www.aseansec.org/4979.htm>>.

<sup>22</sup> Susumu Yamakage, "The Construction of an East Asian Order and the Limitation of the ASEAN Model", *Asia-Pacific Review*, Vol.12, No.2, 2005

<sup>23</sup> Condoleezza Rice, "Remarks at Sophia University" (March 19, 2005)  
<http://www.state.gov/secretary/rm/2005/43655.htm>

<sup>24</sup> "Joint Statement of the Japan-US Security Consultative Committee" (February 19, 2005)  
<http://www.state.gov/r/pa/prs/ps/2005/42490.htm>

Second, the East Asian community will challenge the flexibility of bilateral “hub-spokes” systems thus to increase the transaction cost in both security and economic relations. Third, the East Asian community might serve as an excuse to delay the democratic transition of authoritarian regimes in the region by introducing an Asian model of governance. With these factors, the US seems to have rejected to apply the analogy of trans-Atlantic relations, where NATO and EU play the complementary role. The logic became more clear when US tries to emphasize the trans-Atlantic relations as “community of democracies,” in contrast to the trans-Pacific relations.

### *Japan*

Japan had long been reluctant to engage in any kind of bilateral FTAs, but seeing the emergence of increasing complex network of FTAs throughout the world, finally decided to start seriously focusing on the conclusion of an FTA agreement. The first country with which Japan did so was Singapore, which had few sensitive export products to Japan. The negotiations started in October 2000 and were concluded by January 2002 when Prime Minister Koizumi visited Singapore. In his policy speech delivered in Singapore, Koizumi proposed to create a ‘community that acts together and advances together.’<sup>25</sup> In the subsequent summit in Phnom Penh, ASEAN and Japan issued a ‘Joint Declaration on the Comprehensive Economic Partnership’ (CEP), and in the 2003 summit, they concluded a ‘Framework for Comprehensive Economic Partnership.’ As building blocks to establish a Japan-ASEAN CEP, bilateral FTA negotiations were started in December 2003 between Japan and Thailand, between Japan and the Philippines, and between Japan and Malaysia. Japan and South Korea also agreed to start bilateral FTA negotiations in 2003. Since then Japan has also acceded to the Treaty of Amity and Cooperation (in 2004) but still remains far behind China in terms of bilateral agreements, treaties and memoranda with ASEAN.

In 2002 Policy Speech, Prime Minister Koizumi mentioned Australia and New Zealand as potential partners in ‘expanded’ East Asian community, suggested the potential enlargement of the concept of East Asia. Since Japan has become a late comer, however, in the bilateral FTA dynamics especially with ASEAN member states, it has been fallen behind to find new core attachment to develop relations with ASEAN, notably the TAC accession. Japan’s failure to make concessions to the ASEAN nations in the course of trade liberalization negotiations has also slowed the progress of economic partnership.<sup>26</sup>

Japan’s stance towards East Asian Community became clearer when the Japanese government floated the “Issue Paper” at ASEAN+3 Foreign Minister’s Meeting in June 2004.<sup>27</sup> In the Issue Paper, the Japanese government reaffirmed the importance of enhancing regional cooperation, and analyzed that 1) ASEAN’s leading role in community building, 2) functional cooperation plays the prominent role, 3) ASEAN+3 should involve other regional actors, and 4) ASEAN+3 should continue to articulate principles such as openness, transparency, inclusiveness and conformity with global norms and systems.<sup>28</sup>

The Japanese government also raised points to clarify regarding the modality of East Asian Summit in the “Issue Paper”. Especially, 1) fundamental objective of the East Asian Summit, 2) difference between East Asian Summit and ASEAN+3 Summit, and 3) organization of East Asian Summit have been repeatedly mentioned in question format. By laying out these agendas, the Japanese government seek to have the Summit which could be compatible to 1) Japan’s security commitment with the United States, 2) Japan’s

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<sup>25</sup> <<http://www.mofa.go.jp/region/asia-paci/pmv0201/speech.html>>.

<sup>26</sup> Susumu Yamakage, *ibid*.

<sup>27</sup> “Issue Papers provided by the Government of Japan” (25 June, 2004)

<http://www.mofa.go.jp/region/asia-paci/issue.pdf>

<sup>28</sup> *Ibid*.

economic engagement in this region and APEC/WTO process, and 3) promoting openness and inclusiveness of the Summit process.

## **East Asian Summit and East Asian Community**

### ***Political Process of East Asian Summit I: Modality A and A'***

Another item on the agenda for East Asian countries is the commencement of East Asian Summit. The issue, which was virtually put on the shelf after the proposal of EAVG, was materialized by holding the first East Asian Summit in December 2005. The original idea of EAS derived from the EAVG proposals, then by EASG as a medium and long term goals. However, Malaysia, who happened to be the host country of APT in 2005, strongly wanted to pursue this goal because they had a legacy of EAEC in early 1992, they wanted this concept in their hands.

The earlier thoughts on East Asian Summit were not conceptualized fully to create a new regional framework. Rather, it was more like upgraded version of ASEAN+3 process replaced by renamed as “East Asia.” But several considerable challenges and political struggles came across, before/during the ASEAN+3 Vientiane Summit in 2004.

China has made clear its hope to hold the Second East Asian Summit in 2007, a year before the Beijing Olympic. With coordination with Malaysia, both countries tried to set the modality as: 1) East Asian Summit should be held once in two years, 2) ASEAN and non-ASEAN countries may host in rotation, 3) its membership will be ASEAN+3 (***Modality A***). In response to the Chinese proposal, Japan raised an additional proposal which tried to transform from single Chair to Co-Chair system comprised of ASEAN and non-ASEAN countries, and Japan wanted to co-chair with Malaysia at the first Summit (***Modality A'***)<sup>29</sup><sup>30</sup>.

As for the membership issue, Beijing—eager to entrench its influence over and even dominance of this regional forum from the outset—wished to restrict participants to Southeast and Northeast Asian states (that is, the existing ASEAN+3 members). But Tokyo favored a more all-encompassing grouping in which China’s power and influence would implicitly be balanced by the presence of extra-regional stakeholders, most importantly the United States.

Neither Modality A nor A', however, worked out. At the ASEAN+3 Vientiane Summit in 2004, Philippines strongly opposed to both ideas since Philippines were to be scheduled to host the ASEAN+3 Summit in 2007 (until Myanmar declines its chairmanship in 2006), which makes conflict between hosting of ASEAN+3 and East Asian Summit at the different venue. Certainly, Philippines thought that ASEAN+3 process would be diluted and lose the influence as a Chair.

Indonesia, and to some extent, Vietnam and Myanmar opposed to the idea of Modality A/A' at the Vientiane Summit, because they thought that the ASEAN could be marginalized in the East Asian Summit process, since the +3 countries may have stronger influence over it. They thought that it might be not too wise to create the framework which would lose the ASEAN's grip. They insisted that the integration process

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<sup>29</sup> At the “Issue Paper” proposed by the Japanese government, Japan promoted the “double-track” approach to invite Australia and New Zealand as a “dialogue partner”. “In this case, an EAS would consist of both a ‘core session’ held by ASEAN+3 alone and an ‘expanded session’ in which both ASEAN+3 and regional partners would participate. In the ‘core session’, ASEAN+3 would discuss key issues related to community building. In the ‘expanded session’, ASEAN+3 would brief the regional partners of their discussions in the core session. Other wider issues could also be discussed in the ‘expanded session’. Ideas from experiences in the PMC could be drawn upon in arranging the ‘expanded session’” Japan Ministry of Foreign Affairs, *Issue Paper* (June 2004)

<sup>30</sup> On the ground of policy planning, the Ministry of Foreign Affairs thought that China may have a bigger bargaining power to obtain the role of Chair, since Japan has already had Japan-ASEAN Special Summit Meeting in December 2003. Interview with MoFA officials (August 2004).

of ASEAN should come first.

Japan was positive but with having certain level of ambivalence about East Asian Summit. Its original position was that East Asian groupings should include countries like Australia and New Zealand, since Japan attach importance of these liberal democracies. APT would become a process for further independence of financial cooperation, trade and investment but if it is upgraded to East Asian Summit, they claimed that countries beyond ASEAN+3 should be included at least as dialogue partners.

### ***Political Process of East Asian Summit II: Modality B***

Then, there were important sea change in the spring of 2005 when every country tried to seek for an agreeable modality of the East Asian Summit. Singapore started to think that India, who has been claiming to become a member of East Asian Summit, should not be ignored due to their rapid economic growth. Singapore, Vietnam and Indonesia began proposing that Australia and New Zealand could be invited with different reasons in their mind. For Singapore and Indonesia, their prosperous neighbors are also in down-under. For Vietnam, it might also be beneficial for them to counter-balance Chinese influence in the region, then to give ways to introduce resources and funds from multiple nations.

Meanwhile, ASEAN came up to consensus of inviting Australia, New Zealand and India as full-fledged members, not as a observer or dialogue partner. During the process, ASEAN has created the three criteria for participation for East Asian Summit and floated to other +3 members. These are, East Asian Summit members should 1) have close relations with ASEAN, 2) be a full-dialogue partner with ASEAN and 3) be the signatory of the Treaty of Amity and Cooperation (TAC) (***Modality B***).

With the Modality B becoming the least common denominator, ASEAN once again became the center of the community building process, and was seen to be expanded into wider East Asian Summit process. The annual meeting of the East Asian Summit shall be organized by the ASEAN Secretariat in consultation with the other members. Eventually, ASEAN member states, and other members of the Summit have agreed that ASEAN shall host the annual meetings of the East Asian Summit, which will be held in conjunction with the ASEAN Summit annual meeting. Thus, the East Asian Summit will be held under the chairmanship of ASEAN.

The decision to invite Australia and New Zealand as a formal member to the Summit was part of an attempt by Singapore, Indonesia and Vietnam with having a full support, shortly afterwards by Japan<sup>31</sup>. The ASEAN countries demanded Australia sign a Treaty of Amity and Cooperation as a precondition for being invited. The Howard government was at first reluctant to sign the treaty but decided it was a modest concession compared to the benefits of being a founding member of the new summit conference<sup>32</sup>. Australia has gained formal admission into the East Asian Summit by acceding to the TAC. Alexandra Downer,

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<sup>31</sup> As stated in the footnote 27, Japan's position until early 2005 was to invite Australia and New Zealand as 'dialogue partners' not as full-fledged members.

<sup>32</sup> In a speech on 1 December 2005, Australia's Minister for Foreign Affairs Alexander Downer suggested that the character and direction of the East Asia Summit may take some time to become apparent but welcomed the fact that Australia would be an inaugural participant. Mr. Downer stated that "This is just the first meeting and nothing is set in stone. And if there is to be an emergence of an East Asian community, it will not, in my view, be built around one institution or meeting. An East Asian community will emerge for practical reasons, not for ideological reasons. APEC, the ASEAN Regional Forum, ASEAN plus three, and the East Asia Summit will all contribute to an open but increasingly integrated region..." "The East Asia Summit is only in its very first iteration and will take some time to bed down. But we can say now that we have a regional architecture that serves Australia's interests well. It is open and inclusive. It addresses security and economic issues in a practical way and Australia has a very strong voice in how it develops." Frank Frost and Ann Rann, "The East Asian Summit: Issues and Outcomes" Australian Parliamentary Library E-Briefs, 17 January, 2006.

Australia's Foreign Minister, said Australia would be keen to participate in the East Asia Summit, although some countries have opposed its membership. Australia has long baulked at signing the TAC claiming it could conflict with obligations under its security treaty with the US. Some Asian countries also regard India's membership of the group as a further balance to China. The Indians have traditionally not been active in the region because of isolationist economic policies but as a result of the market opening policy which began fourteen years ago they now want to pursue engagement with East Asia<sup>33</sup>.

### **Conclusion: Emergence of Dual Image of East Asian Community: Whither ASEAN+3 or East Asian Summit?**

The 16 participants in the first East Asia Summit met on 14 December 2005. The meeting was relatively short (lasted three hours) and few specific decisions were made: the emphasis was on developing communication among the members. Malaysia's Prime Minister Badawi, the chair for the meeting, in his Chairman's Statement described the Summit as a 'leaders-led' gathering that initiated confidence-building among the members as a first step towards more substantial collaboration.

The main issues discussed during the Summit included the need for denuclearization of the Korean peninsula, terrorism, avian flu, sustainable development, the need for progress in the Doha round of WTO negotiations and the role which the EAS should play as a complement to existing cooperation dialogues (including ASEAN+3) in the process of community building in the region.

The 'Kuala Lumpur Declaration on the East Asian Summit' indicated that it will be a 'forum for dialogue on broad strategic, political and economic issues of common interest and concern, and with the aim of promoting peace, stability and economic prosperity in East Asia'. It affirmed that the East Asian Summit is intended to be an 'open, inclusive, transparent and outward-looking forum, in which we strive to strengthen global norms and universally recognized values, with ASEAN as the driving force working in partnership with other participants of the East Asia Summit'. The Summit would be 'convened regularly', would be hosted and chaired by an ASEAN member and would be held 'back to back with the annual ASEAN Summit'. The Summit participants issued a specific declaration concerning avian flu, with a commitment to report all outbreaks rapidly and transparently, and to take steps to ensure that the disease does not develop into a form which could be transmitted directly between humans.

The existence of multiple and even competing forms will allow the core group of East Asian countries to retain the leadership role in driving regional integration. At the same time, it will allow them to accommodate interests from outside the region to a certain extent, thereby reducing possible misgivings about an East Asian community evolving into an exclusive bloc.

Whether or not the newly launched East Asia Summit will play a central role in regional integration in the future, its occurrence points to potentially bright prospects for the East Asian community. It will be a very different, but possibly even more successful, model of regionalism from those we have seen so far in other parts of the globe.

A large part of the original rationale for bringing together leaders from across East Asia was to lay the foundations for an institutionalized, pan-regional community with both economic and security dimensions. The precise ambit of such a community, let alone its modus operandi, is still undefined. As with the East Asian Summit, greater attention has focused on the community's potential membership. While India and Japan have continued to favor using the East Asian Summit, with its wider membership, as the basis for a community, it was clear that once the summit's membership had diversified to include non-East Asian states, China could only accept the more exclusive ASEAN+3 as the basis for a regional community. This

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<sup>33</sup> David Hale, "The East Asian Summit", Asia Media, December 12, 2005.

Chinese prescription, based essentially on power-political reasoning, finds some sympathy in states like Malaysia and Thailand.

While the Kuala Lumpur Declaration at the end of the summit failed to indicate what part, if any, the EAS might play in establishing the regional community, informal remarks by the summit chairman indicated that he did not see Australia, India and New Zealand as future members of it. Nevertheless, in practical terms these three states are increasingly integrating with East Asia and possess in Japan a major East Asian ally. Their aim will be to join a regional community primarily concerned with facilitating trade and investment, and like Japan they will not want to be part of any grouping that China might attempt to use as a vehicle for regional domination. A larger question concerns the extent to which an East Asian community, whether its membership be inclusive or exclusive, might be able to achieve significant consensus on economic and security issues given the fundamental rivalries that exist amongst combinations of major players such as China and Japan, and China and India.

## **Appendix: A**

### ***Kuala Lumpur Declaration (East Asian Summit)***

SHARING the view that the East Asia Summit could play a significant role in community building in this region;

FURTHER RECOGNISING the need to support efforts to build a strong ASEAN Community which will serve as a solid foundation for our common peace and prosperity;

DO HEREBY DECLARE:

FIRST, that we have established the East Asia Summit as a forum for dialogue on broad strategic, political and economic issues of common interest and concern with the aim of promoting peace, stability and economic prosperity in East Asia.

SECOND, that the efforts of the East Asia Summit to promote community building in this region will be consistent with and reinforce the realisation of the ASEAN Community, and will form an integral part of the evolving regional architecture.

THIRD, that the East Asia Summit will be an open, inclusive, transparent and outward-looking forum in which we strive to strengthen global norms and universally recognised values with ASEAN as the driving force working in partnership with the other participants of the East Asia Summit.

FIFTH, that:

Participation will be based on the criteria for participation established by ASEAN;

The East Asia Summit will be convened regularly;

The East Asia Summit will be hosted and chaired by an ASEAN Member Country that assumes the ASEAN Chairmanship and held back-to-back with the annual ASEAN Summit; and

The modalities of the East Asia Summit will be reviewed by ASEAN and all other participating countries of the East Asia Summit.

### ***Chairman's Statement (ASEAN+3 Summit)***

2. We signed the Kuala Lumpur Declaration on the ASEAN Plus Three Summit to reaffirm our commitment to ASEAN Plus Three cooperation, which has achieved substantial progress in the last eight years. We agreed to continue holding the ASEAN Plus Three Summit annually in conjunction with the ASEAN Summit to guide and provide political momentum to East Asian cooperation and community building efforts.

3. We agreed that the ASEAN Plus Three process will continue to be the main vehicle in achieving that goal, with ASEAN as the driving force, and with the active participation of the ASEAN Plus Three countries, in order to promote shared ownership. We reiterated our common resolve to realise an East Asian community as a long-term objective that would contribute to the maintenance of regional and global peace, security, progress and prosperity

16. We welcomed the convening of the first East Asia Summit (EAS) on 14 December 2005 in Kuala Lumpur, Malaysia. We shared the views that the EAS should be convened annually and that the EAS will play a significant role in this region. The EAS will be consistent with and reinforce ASEAN's efforts in building the ASEAN Community. We recognised that the EAS will contribute to the evolving regional architecture. We look forward to a fruitful deliberation of the EAS.

# East Asian Summit Political Process I

## 【Modality A】(Oct 2004)

2005 Host C: Malaysia  
2007 Host C: China  
(Chinese Proposal)

Bi-Annual Meeting  
Alternative Host: ASEAN / Non-ASEAN  
Membership: ASEAN + 3  
ASEAN+3 Summit Coexist

## 【JPN Counter Proposal】(July 2004~March 2005)

- 1) East Asian Summit should be Co-hosted by ASEAN and Non-ASEAN Member States. The First Meeting in Kuala Lumpur should be Co-hosted by Malaysia and Japan
- 2) Australia and NZ should be invited to EAS as Dialogue-Partners (two-tier approach)

## 【Philippines' Response】

Philippines will be a chair country for ASEAN in 2007. If China holds EAS in 2007, ASEAN+3 Summit in Philippine will be deteriorated. (cf. Myanmar has given up their chairmanship in 2006)

## 【Indonesian Response】

ASEAN should focus on ASEAN-integration rather than EAC (SBY)

# East Asian Summit Political Process II

## 【Modality B】(April 2005)

2005 Host C: Malaysia  
2006 Host C: ASEAN

**Mod B. Proposal**  
Singapore  
Indonesia  
Vietnam

## 【Criteria on EAS Membership】

- 1) Dialogue Partner of ASEAN
- 2) Accede Treaty of Amity and Cooperation in Southeast Asia (TAC)
- 3) Having Substantive Relations with ASEAN

New Member: Australia, New Zealand, India

ASEAN+3+3 = 16 Member States

## Additional Support

## 【JPN Counter Proposal】(July 2004~March 2005)

- 1) East Asian Summit should be Co-hosted by ASEAN and Non-ASEAN Member States. The First Meeting in Kuala Lumpur should be Co-hosted by Malaysia and Japan
- 2) Australia and NZ should be invited to EAS as Dialogue-Partners (two-tier approach)

## 【Modality A】(Oct 2004)

2005 Host C: Malaysia  
2007 Host C: China  
(Chinese Proposal)

Bi-Annual Meeting  
Alternative Host: ASEAN / Non-ASEAN  
Membership: ASEAN + 3  
ASEAN+3 Summit Coexist

## 【Agreed Modality】

- 1) Participation will be based on the criteria for participation established by ASEAN
- 2) The East Asia Summit will be convened regularly
- 3) The East Asia Summit will be hosted and chaired by an ASEAN Member Country

## 2. Trade and FDI Driven Economic Growth and Regional Economic Integration in East Asia<sup>1</sup>

*Prof. URATA Shujiro*

*Professor*

*Waseda University*

### I. Introduction

East Asia achieved remarkable economic growth until it was suddenly struck by the economic crisis in the late 1990s. Although East Asia experienced devastating setback from the crisis, many East Asian economies quickly recovered to achieve reasonable economic growth. Rapid economic growth in the pre-crisis period and quick recovery in the post-crisis period by East Asian economies are attributable to various factors such as sound macroeconomic management, availability of low-wage labor and others. Among these factors the role of foreign trade and foreign direct investment (FDI) has to be emphasized.

FDI recipient countries can gain various benefits from receiving FDI, which would contribute to economic growth. FDI brings various resources such as funds for fixed investment, technology, and management know-how, which are in acute shortage in many developing countries. In addition, FDI enables recipient countries to utilize sales and procurement networks of multinational corporations (MNCs), major foreign investors, to result in the expansion of trade (exports and import). Export expansion promote economic growth as it enables exporting countries to earn foreign exchange, which can be used to import technology, intermediate goods, capital goods, and other items for achieving economic growth. Successful export performance in turn results in attracting FDI with an export motive. This way a trade-FDI nexus is formed in East Asia, to result in increasing intra-regional economic activities, or deepening regionalization. What has been remarkable in East Asia is sequential formation of the trade-FDI nexus engaging at first in the early 1980s two East Asian Newly Industrializing Economies (NIEs), Singapore and Hong Kong, which were followed by four members of the Association of Southeast Asian Nations (ASEAN4), or Indonesia, Malaysia, the Philippines, and Thailand in the latter half of the 1980s. In the 1990s China joined other East Asian countries to be a part of the trade-FDI nexus in the region. Such sequential evolution of the trade-FDI nexus resulted in multi-layered development process in East Asia. One special characteristic of trade-FDI nexus in East Asia is that such nexus is built on regional production and distribution network by MNCs from not only East Asia but also from other parts of the world including the US and the EU.

Up against market-driven regionalization resulting from rapid trade and FDI expansion, which was attributable to trade and FDI liberalization, East Asia started to witness institution-driven regionalization in the forms of regional cooperation such as the Chiang-Mai initiative, which is a currency swap arrangements to deal with the shortage of foreign exchange involving East Asian countries and free trade agreements (FTAs). These developments seem to have shifted the gravity of regionalization from market forces to regional institutions.

In light of these new developments in East Asia, this paper analyzes the changing nature of regionalization and it further attempts to present several important policy issues in East Asia in order to maintain its economic dynamism in the future. The remainder of the paper is organized as follows. Section II

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<sup>1</sup> Prepared for the 2<sup>nd</sup> International Workshop on “An East Asian Community and the United States” June 20-21, 2006, Tokyo.

examines the market-driven regionalization, which is created by rapid expansion of foreign trade and FDI. Section III expands the analysis of market-driven regionalization by explicitly shedding light on regional production and distribution networks developed by MNCs. Section IV turns to the issue of institution-driven regionalization, and finally section V presents some concluding remarks on the challenges that East Asia faces to achieve further economic growth.

## **II. Expansion of Foreign Trade and Foreign Direct Investment in East Asia**

East Asia saw rapid expansion of foreign trade and FDI in the 1980s and in particular 1990s, indicating the increasing importance of international economic activities in their economies. Between foreign trade and FDI, FDI inflows expanded particularly fast during the 1990s. Rapid expansion of foreign trade and in particular FDI inflows can be seen from Figure 1, where exports and FDI inflows are shown with GDP for East Asia. From 1980 to 2002 GDP for East Asia increased five-fold, while exports increased approximately eight-fold. FDI inflows increased remarkably 40-fold from 1980 to 2000, after which they declined. This section examines recent developments of foreign trade and FDI in East Asia.

### **II.1. Foreign Trade**

Foreign trade of East Asian economies increased rapidly and continuously in the 1980s and 1990s with a decline in 1998 as a result of the financial crisis (Table 1). In 23 years between 1980 and 2003 merchandise exports and imports of East Asian economies (excluding Japan) increased 6.9- (10.3-) and 5.9- (9.3-) fold, respectively. Since both world exports and imports only increased 3.3-fold each during the 1980-2003 period, the shares of East Asia in world exports and imports increased from 12.8 (6.3) and 13.3 (6.4) percent to 23.5 (17.3) and 20.6 (15.7) percent respectively. It is to be noted that exports grew faster than imports for East Asia, indicating that increased global linkage through foreign trade contributed to the increase in GDP as well as foreign exchange earnings. As shown in Table 2 Among East Asian countries, excluding Cambodia and Vietnam, whose growth performance is exceptional partly because of their low base, China registered especially high rate of growth, as its exports and imports increased 24- and 21-fold over the 1980-2003 period, respectively. China was followed by Thailand, Hong Kong, Korea and others

For many East Asian countries foreign trade grew faster than GDP during the 1980-2003 period, resulting in increased linkage to global economy. Specifically, exports-GDP and imports-GDP ratios for East Asian countries increased from 27 and 28 percent in 1980 to 46 and 43 percent in 2003, respectively (Table 1). It is remarkable to note that for all the East Asian countries listed in Table 2 the export-GDP and import-GDP ratios are higher than their respective world averages in 2002.

Remarkable expansion of foreign trade was accompanied by various changes in the structure of foreign trade in East Asia. Table 3 shows export destinations and import sources for East Asian countries. One remarkable development is the increased importance of East Asian countries both as export destinations and as import sources, indicating increased intra-regional trade in East Asia<sup>2</sup>. For East Asian countries as a whole the share of exports destined to East Asia in their total exports increased from 22.1 percent in 1980 to 40.1 percent in 2002.

Turning to the import sources of East Asian countries, the importance of East Asia increased, similar to the pattern observed for their export destinations. For East Asian countries as a whole, the share of imports

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<sup>2</sup> This pattern was detected by many studies including Urata (2001a) and Kawai and Urata (2004).

from East Asia in their total imports increased from 22.2 percent in 1980 to 45.9 percent in 2002. A comparison of the findings on export patterns and import patterns shows that for East Asia, East Asia is more important as an import source rather than an export destination. This observation reflects the patterns of trade and production, in which East Asian countries procure parts and components from other East Asian economies to produce final products to be exported to non-East Asian economies such as the US and the EU. This “triangular trade” pattern indicates the role of East Asia as a world factory, which produces products not only for East Asia but for other parts of the world.

Commodity composition of foreign trade for East Asian countries changed dramatically (Table 4). One particularly notable development was rapid increase in the share of manufactures in total exports for four Association of Southeast Asian Nations (ASEAN4) countries (Indonesia, Malaysia, Philippines, and Thailand). Among manufactures, electronic products show interesting developments. The NIEs had relatively high share of electronics in total exports already 1980s and then they increased their shares in the following periods. Malaysia and Thailand increased their shares in the 1980s, while the Philippines and China increased their shares in the 1990s. These sequential developments of the increasing importance of electronics exports for East Asian economies are the essence of multi-layered development process, resulting from the formation of the trade-FDI nexus, which will be discussed later.

These observations may indicate that many East Asian countries are large exporters of high-tech products such as electronics products, but one should note that many countries are engaged in labor-intensive production process such as assembling of high-tech products rather than in high tech-intensive production process such as development of new products. Recognizing this point, one may argue that East Asian countries have a comparative advantage in labor-intensive processes of high-tech products but not in high-tech intensive processes. We will examine this point again, when we examine regional production network in the section on trade-FDI nexus.

Although not shown in the table, it is interesting to note that light manufactures such as textiles, clothing, and other consumer goods accounted for a relatively large share of exports for many countries including China and Hong Kong, reflecting the fact that many East Asian countries still have a comparative advantage in the production of these products.

When compared to dramatic change in the pattern of exports observed above, the change in the pattern of imports was less pronounced, as the share of manufactures in total imports for many East Asian countries remained around 60-80 percent throughout the 1980-2003 period. Despite more or less stable share of manufactures in total imports, there was a marked change in the compositional shares of imports among different manufactures. Specifically, electronics increased their shares for many economies similarly to the pattern observed for exports.

Increasingly high shares of electronics products in both exports and imports for East Asian countries suggest the expansion of intra-industry trade in these products among the East Asian countries.

## **II.2. Foreign Direct Investment**

Foreign direct investment (FDI) inflows in East Asia started to increase in the latter half of the 1980s (Figure 1 and Table 5). After a short period of stagnation in the late 1980s and early 1990s largely because of the world recession, they started to rise again in the mid-1990s as the world economy recovered from the recession. The rate of increase accelerated in the mid-1990s before reaching a peak in 1997. FDI inflows declined in 1998 because of the financial crisis, but they recovered quickly to reach a record high level in 2000. FDI inflows to East Asia declined sharply in 2001 largely because of the decline in the world

economy, which in turn was attributable to the bursting of the IT (information technology) bubble and the terrorists' attacks.

One observes a sequential pattern of expansion of FDI inflows for the NIEs, ASEAN4, and China from the mid-1980s to early 2000s. FDI inflows to NIEs expanded rapidly first before those to ASEAN4 or China in the latter half of the 1980s, and then toward the end of 1980s FDI inflows to ASEAN4 began to increase notably (Figure 2). Finally, FDI inflows to China saw a sharp increase in the early 1990s and surpassed ASEAN4 and the NIEs. Divergent trends started to show toward the end of the 1990s, as FDI inflows to the NIEs and China continued to increase while FDI inflows to ASEAN4 started to decline.

Expansion of FDI inflows in East Asian developing countries resulted in the increased importance of MNCs in economic activities for these countries. Such development can be confirmed by the increase in the FDI inflows-GDP ratio for many countries in Table 5.

Let us examine the changing patterns of FDI inflows to East Asian developing countries from four different perspectives; source countries, sectoral composition, sources of finance, and types of FDI.

Table 6 shows the changing patterns of FDI source countries for the selected East Asian developing countries. Unlike the pattern of increasing importance of intra-regional dependence observed for many countries concerning foreign trade, the patterns of FDI sources as well as their changes do not appear to show any such patterns for many East Asian countries. Indeed, the importance of intra-regional FDI in total FDI in East Asia declined in several countries from 1990 to 2002, largely reflecting a decline in the importance of FDI from Japan. Although one can not detect a clear tendency of increasing importance of developing East Asian countries in FDI inflows in developing East Asian countries in terms of proportions shown in Table 7, it is important to note the increasing importance of FDI from developing East Asian countries in absolute terms because FDI inflows to East Asian developing countries increased substantially<sup>3</sup>.

Concerning the sectoral patterns of FDI inflows, one common feature is high and increasing importance of electronics industry in either overall FDI or manufacturing FDI for many East Asian developing countries (Table 7). Among them very high shares of electronics are recorded for Malaysia and Singapore. For Malaysia the share of electronics in total manufacturing FDI inflows fluctuated around 20 to 50 percent in the 1990s, but since the end of 1990s, the share remained high around 50 percent. For Singapore, electronics maintained consistently high shares around 40 to 50 percent of total FDI. Korea and Taiwan also witnessed rapid increase in the share of electronics industry in manufacturing or total FDI. The share for China is significantly lower compared to others, because FDI inflows in services such as real estate are very large. A possible inconsistency in Chinese FDI statistics should be mentioned here, as a substantial part of FDI inflows are not registered in any specific sectors, but they are included in "others."

### **III. The Emergence of MNC-Driven Regional Production Network**

We have seen rapid expansion of foreign trade and FDI flows in East Asia since the mid-1980s. The speed of expansion was particularly fast in the 1990s and particularly for FDI inflows. Indeed, foreign trade and FDI flows expanded at tandem by forming virtuous spirals between them. There are several reasons why they are closely related in East Asia. Realizing that FDI brings in various benefits including the use of well-developed international sales/export networks of foreign firms and that export expansion would promote economic growth, many East Asian economies pursued policies to attract FDI and promote export, as we will see below. Faced with an expanded opportunity to exploit comparative advantages in East Asian countries

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<sup>3</sup> It should be noted that substantial FDI was withdrawn from Thailand in 2002, reflecting in the negative values shown for FDI inflows from the US and the EU.

under favorable trade and FDI environment, cost-conscious foreign MNCs actively undertook FDI in East Asian countries. Such FDI resulted in successful expansion of exports from these export bases in East Asia. The countries that succeeded in expanding exports in turn attracted FDI, because they were seen as capable of providing an environment conducive to efficient production. In this way, virtuous spirals of export expansion and FDI expansion, or the FDI-trade nexus, were formed. Indeed, rapid expansion of FDI inflows resulted in the creation of regional production networks in machinery sectors, especially in electronics sector. This section examines the trading behavior of Japanese MNCs and the creation of regional production network in electronics sector.

### **III.1. Trading Activities of Japanese MNCs**

An examination of Asian affiliates of Japanese MNCs reveals an increased outward orientation and increased intra-regional orientation (Table 8).

For Asian affiliates of Japanese MNCs, the share of local sales and local procurement in their respective total declined from 1992 to 2001. This change is particularly notable for the sales patterns. This trend seems attributable to opening up of the host countries in trade policies, to which the affiliates responded.

The increased intra-regional orientation can be found as the share of sales destined to other Asian countries under the category “Asia” increased from 11.2 percent in 1992 to 18.3 percent in 2001. Increasing intra-regional trade by the affiliates of Japanese MNCs appears to result from at least two forces. One is the establishment of free trade areas such as the North American Free Trade Agreements and the Mercosur in Latin America. Faced with lowering trade barriers in FTA members, the affiliates expanded trade with FTA members.

Another factor is the emergence of regional production and distribution network, under which MNCs break up the production process into several sub-processes and locate a sub-process in a country, where that particular sub-process can be conducted most efficiently. Such inter-process division of labor strategy, which has been adopted by many MNCs in electronics, transportation, precision machineries as well as textiles, increased intra-regional trade by MNCs. We will examine the emergence of inter-process, intra-regional trade in East Asia in a later section.

An increasingly large portion of affiliates’ transactions take the form of intra-firm trade for the Asian affiliates of Japanese MNCs (Table 9). The share of intra-firm transactions in overall transactions increased sharply from 1992 to 2001. In 1992 intra-firm trade was substantial for the affiliates’ trade with the home country, or Japan, indicating a strong relationship with parent company in Japan. However, in 2001 intra-firm transactions amount to a large part of affiliates’ transaction not only in their trade with home countries but also in their transactions in the host countries and those with foreign countries. The increase in intra-firm transaction by the affiliates of Japanese MNCs appear to indicate the emergence of regional production network involving Japanese MNCs, which has been made possible by the increase in the number of affiliates and by the expansion of their activities.

The findings on high trade-orientation of Asian affiliates of Japanese MNCs and those on their high shares of trade inside Asia appear in some sectors including electronics and general machineries appear to indicate the presence of inter-process trade involving parts and components. This is the subject of investigation in the next section.

### **III.2. The Emergence of Regional Production Networks**

An earlier observation of the sales and procurement patterns of Asian affiliates of Japanese and US MNCs suggests the formation of regional production network in electronic industry, under which parts and components are traded internationally to be assembled to produce final products in East Asia<sup>4</sup>. This section investigates the formation of regional production networks in East Asia by examining data on foreign trade and production.

East Asia has become a major production site for electronics products in the world since the 1980s<sup>5</sup>. As the discussions in the previous sections indicate, a large part of electronics production in East Asia are undertaken by foreign companies from various parts of the world, although in recent years local producers have increased their production sharply.

Many foreign electronics companies have set up regional production system in East Asia by adopting a fragmentation strategy, under which production process is divided into several sub-processes and each sub-process is located in a country where that sub-process is conducted most efficiently or at the least cost through FDI. For example, the production process of a personal computer (PC) is divided into design, production of parts, assembling of finished products (PCs)<sup>6</sup>. A typical Japanese PC producer undertakes design in Japan, and assigns production of various parts to different countries, and assembles PCs in China by importing parts from different locations. As for parts production, for example, the following part-country assignment is set up, HDD-the Philippines, CPU-the US, memories-Korea, and Crystal Liquid Display-Taiwan, depending on the suitability of the locations for the production of particular parts.

Foreign electronics producers have adopted the fragmentation strategy for several reasons. One is standardization of production process, which only requires assembling of components without sophisticated technologies. Another reason is low tariff rates on components trade partly because of EPZ arrangement adopted by several countries in East Asia. Information Technology Agreement (ITA) under the WTO, under which developed and developing members agreed to remove tariffs on IT products by 2000 and 2005, respectively, has contributed to the reduction of tariffs on IT products. Let us examine how international trade in electronics is conducted in East Asia below.

Table 10 shows the proportion of components trade in overall (components and finished products) trade in electronic products. Several interesting observations may be obtained from the table. First, trade in electronics components account for a large share of electronics trade for East Asian countries. Specifically, electronics components account for approximately 65 and 75 percent of East Asia's overall electronics exports and imports with the rest of the world, respectively, while the corresponding ratios for the world trade is significantly lower at 55 percent. Second, the proportion of components trade is particularly high for intra-East Asian trade. These two findings indicate the formation of regional production system in East Asia, where components are traded for the production of final products in East Asia.

### **IV. Changing Policy Environment: Liberalization of Trade and FDI policies<sup>7</sup>**

The factors behind the notable expansion in foreign trade and FDI inflows in East Asia fall into two groups, one concerning domestic factors and the other concerning external factors. The most important

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<sup>4</sup> Kimura and Ando (2004) found that large part of machinery trade in East Asia is composed of parts and components, providing an evidence for the formation of regional production network.

<sup>5</sup> Takeuchi (2004) analyzes the development of electronics industry in East Asia by focusing on trade and FDI.

<sup>6</sup> For details, see Takeuchi (2004).

<sup>7</sup> This section extends Urata (2005a)

domestic factor was the liberalization of both trade and FDI policies. In addition, a favorable macroeconomic environment, reflected in relatively stable price levels, predictable and stable business environment and supporting institutions for private sector activity, relatively well-developed infrastructure, together with an abundant supply of well-educated, low-wage labor contributed to the expansion of exports and FDI inflows.

As for the external factors, the substantial realignment of exchange rates, particularly the yen-dollar exchange rate in the mid-1980s, was crucial. It should also be noted that the appreciation of the currencies of the NIEs against the US dollar in the late 1980s promoted FDI outflows from the NIEs to other East Asian countries. In addition, remarkable technical progress in information technology facilitated trade and FDI by reducing the cost of communications. Finally, increased competition among MNCs, which resulted partly from liberalization and deregulation in various sectors in many countries of the world, promoted their global activities, thereby expanding trade and FDI. The remainder of this section examines liberalization in trade and FDI policies in East Asia, which contributed to rapid expansion of trade and FDI in East Asia.

#### **IV.1. Unilateral Liberalization**

In the 1980s and 90s, East Asian economies embarked on unilateral liberalization of trade and FDI policies and deregulation in domestic economic activities as part of more comprehensive structural reform policies. Such policy changes were induced partly by their commitments to the World Bank and the IMF for obtaining economic assistance and largely by the realization on the part of East Asian economies that liberalization and deregulation would promote economic growth. Liberalization of trade and FDI policies led to the expansion of exports and inward FDI because it shifted the incentives from import-substituting production to export production and increased the attractiveness of these economies to foreign MNCs.

East Asian economies unilaterally liberalized their import regimes by lowering tariff rates and non-tariff barriers from the early 1980s through the early 2000s (Table 11). The notable exceptions were Hong Kong and Singapore, which had adopted virtually free trade regime for a long time. In spite of substantial reduction in tariff rates, some economies still maintain relatively high tariff rates. The average tariff rates for Korea and Thailand are around 15 percent in the early 2000s. It should be noted that primary sector is relatively more protected than manufacturing sector, as the average tariff rates for primary products are higher than those for manufactured products in all the economies in the table except Malaysia and Singapore.

In addition to trade liberalization in the forms of reduction in tariff rates and non-tariff barriers, several policies adopted by East Asian countries had similar effects to trade liberalization, promoting exports. One is duty drawback system, which returns tariffs paid on the imported parts and components, which are used for the production of exports, to the producers. This system has virtually the same effect as free trade for the producers of exported products. Another is export processing zones (EPZs), or free trade zones (FTZs), in which exporters or producers of export products can take advantage of free trade on imported inputs..

Policies toward FDI inflows started to be liberalized in the mid-1980s and liberalization of FDI policies has continued since then, because the East Asian economies began to realize that FDI inflows would promote economic growth. Although it is difficult to quantify the restrictiveness of an FDI regime, it is clear that many East Asian economies have liberalized their policies toward FDI inflows since the mid-1980s<sup>8</sup>. Restrictions on FDI take various forms, including restrictions on market access, most-favored-nation treatment, and national treatment. Many East Asian economies reduced restrictions on market access by reducing the number of sectors and industries on the negative list and by relaxing the limits on foreign equity

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<sup>8</sup> Japan PECC (2002) examined the impediments to FDI in APEC economies, and found that many East Asian economies reduced the number and the level of impediments by liberalizing FDI policies.

ownership. Furthermore, recognizing the important contribution that FDI may make toward economic growth, a number of economies introduced incentives such as tax breaks to attract FDI. Indeed, there has been keen competition among the countries in the region to attract FDI by reducing barriers and providing incentives.

#### **IV.2. Liberalization under Multilateral Framework**

Turning to the multilateral level, the Uruguay Round of multilateral trade negotiation under the GATT started in 1986 and ended in 1994. Although the negotiations lasted eight years, twice as long as was targeted, the Uruguay Round made substantial progress toward liberalizing trade and FDI. The achievements include: a reduction in tariff rates; framework agreements on trade in services, on intellectual property rights and on trade-related investment measures; a timetable for phasing out all quantitative restrictions on trade including those on textiles under the Multi-Fiber Arrangement (MFA); first steps toward bringing agriculture more firmly under a multilateral discipline; a stronger dispute settlement mechanism; and the establishment of the WTO. It should be noted that China liberalized its trade regime substantially in order to join the WTO and it has committed itself to liberalize trade further after joining the WTO.

Since the establishment of the WTO in 1995, it took as long as six years to start a new multilateral negotiation. The long delay for the start of the new round was mainly due to the differences in the views toward multilateral trade liberalization between developed and developing members. The Doha Development Agenda (DDA), the first round under the WTO, started in 2001 but it has not entered real negotiation yet because of the differences in opinions on the framework of DDA not only between developed and developing members but also within the respective groups.

#### **IV.3. Liberalization under Regional Framework**

Liberalization of trade and FDI policies also progressed in regional contexts in the 1990s in East Asia. The members of the ASEAN started the ASEAN Free Trade Area (AFTA) process in 1992 to make ASEAN a competitive region for exports and for attracting FDI. The 1992 agreement provided for the liberalization of tariff and non-tariff measures under the Common Effective Preferential Tariffs. The target year for achieving tariff and non-tariff liberalization was originally set for 2008, but was later moved forward to 2002. The AFTA has been in effect among the original five ASEAN members—Indonesia, Malaysia, Singapore, Thailand and the Philippines—since January 2002 when the tariff rates were reduced to 0-5 percent, though the exclusion list is long and individual country circumstances vary. Furthermore, Vietnam is to comply with the same tariff standards by 2003, Laos and Myanmar by 2005, and Cambodia by 2007. By 2010 ASEAN is expected to become a complete free trade area free from tariffs with the exception of CLMV members, which are given later deadlines. FDI liberalization in the ASEAN has been underway after the creation of the ASEAN Investment Area (AIA) in 1998, which provides coordinated investment cooperation and facilitation programs, market access, and national treatment of all industries. But some ASEAN members continue to maintain sizeable sensitive and exclusion lists from FDI liberalization.

Another regional framework that promoted trade and FDI liberalization in East Asia is the Asia-Pacific Economic Cooperation (APEC) forum. This trans-regional forum, which was established to promote economic growth in the region, includes not only East Asian economies but also economies in North and South America and Oceania. Following the Bogor declaration in 1994 calling for full liberalization of trade and FDI by 2010 for developed-economy members and by 2020 for developing-economy members, APEC members agreed to prepare and implement individual action plans specifying near- and medium-term liberalization measures. Peer pressure has played a crucial role in the implementation of liberalization

schemes. All APEC members have made significant progress toward freer trade and FDI regimes.

#### **IV.4. Bilateral and Regional Framework: Recent Surge of FTAs in East Asia**

East Asia was not active in the formation of regional trade agreements (RTAs), which include FTA and customs union, until recently (Table 12)<sup>9</sup>. ASEAN Free Trade Area (AFTA) was the only major FTA until Japan and Singapore enacted Japan—Singapore FTA (formally named a New Age Japan-Singapore Economic Partnership Agreement, JSEPA) in 2002<sup>10</sup>. However, the situation changed dramatically in recent years. Many economies in East Asia began to form FTAs with the countries not only in the region but also outside the region. In light of these developments, one can detect the change in the characteristics of regionalization in East Asia around the turn of the century from market-driven to institution-driven regionalization as the main driver of regionalization is changing from the market forces unleashed by trade and FDI liberalization to regional and bilateral institutions such as FTAs.

Besides AFTA, ASEAN as a group as well as its members individually have become active in FTA discussions with other countries in recent years. One of the FTAs involving ASEAN that has received most attention recently is that with China. ASEAN and China enacted FTA in goods trade in July 2005 and they are currently negotiating FTA in services trade. ASEAN is currently also negotiating FTAs with Japan, Korea and others. Several ASEAN members have become active in establishing bilateral FTAs. Singapore is a frontrunner in this FTA race as it enacted many FTAs with countries such as New Zealand, Japan, Australia, the USA, the EFTA, and India and it is negotiating FTA with a number of countries. Thailand has also become active in establishing FTAs, as it has implemented FTA with Australia, New Zealand, and India, while it is currently under negotiations with the USA, Japan and many others. Malaysia signed FTA with Japan and it agreed to begin negotiations with several countries including the US. Both the Philippines and Indonesia are negotiating FTA with Japan separately.

Compared to ASEAN countries in Southeast Asia, the economies in Northeast Asia including China, Japan, Korea, and Taiwan had not been active in FTAs until recently. However, China, Japan and Korea have become very active in FTAs. China implemented FTA with ASEAN, Hong Kong, Macau, and it is negotiating FTAs with over 20 countries. Japan enacted FTA with Singapore and Mexico. It has signed or is very close to signing FTAs with Malaysia and Thailand, and it is currently in negotiations with ASEAN, Indonesia, the Philippines, Korea, and Chile. Korea implemented FTAs with Chile and Singapore and is in negotiation with Japan, ASEAN and others. It is scheduled to begin negotiations with the US.

An idea of FTA covering East Asian countries has emerged. At the Leaders' summit meeting of ASEAN+3 (China, Japan, and Korea) in 1998 the leaders decided to set up the East Asia Vision Group to study long term vision for economic cooperation. The group has presented the leaders with recommendations including the establishment of East Asia FTA. Currently, the Expert Group, which was set up at the recommendation of ASEAN+3 Economic Ministers, is studying the possibility of East Asian FTA, comprising

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<sup>9</sup> In the GATT/WTO, regional trade agreements (RTAs), which violate one of its basic principles of non-discrimination, are permitted under GATT Article XXIV with several conditions, which include liberalization of substantially all the trade of the members, not increasing trade barriers on non-members, and completing the RTA process within ten years. For developing members, more lenient conditions are applied under the enabling clause. An FTA is considered to be a shallow form of regional integration, because it only removes tariff and non-tariff barriers among the members, while a customs union is a deeper integration, as it adopts common external tariffs on non-members, in addition to the removal of tariff and non-tariff barriers on trade among the members.

<sup>10</sup> AFTA was discussed in an earlier section. For discussions on FTAs in East Asia, see for example, Aggarwal and Urata (2006), Lincoln (2004), Urata (2005b), and Pangestu and Gooptu (2004).

of ASEAN+3.

Despite heightened interests in FTAs by East Asian countries, East Asian countries have faced serious obstacles in reaching an agreement. As one would expect, strong opposition comes from non-competitive sectors, which are subject to competition from FTA members. Besides, some East Asian countries have political, historic, and other kinds of problems. As such, a number of FTA negotiations have been stalled.

Various reasons can be considered behind the recent surge of FTAs in East Asia. First, rapid expansion of FTAs in other parts of the world has made East Asian economies recognize the importance of establishing FTAs in order to maintain and expand their export opportunities. Indeed, the number of FTAs reported to the GATT/WTO by its members started to expand sharply since the early 1990s and the pace of the expansion accelerated in the mid-1990s when the WTO was established. Second, a stalemate of the negotiations under the DDA turned the attention of the WTO members with an interest in trade liberalization to FTAs. Third, the Asian financial crisis in 1997-98 prompted East Asian economies to realize the need for regional cooperation such as FTAs in order to avoid another crisis. Fourth, rivalry among East Asian economies over gaining a leadership role in the region has activated their FTA strategies.

One notable characteristic of FTAs in East Asia is their comprehensiveness in coverage. As such, some of the FTAs established in East Asia are named Economic Partnership Agreement (e.g. Japan-Singapore EPA, JSEPA), or Closer Economic Partnership Agreement (e.g. China-Hong Kong CEPA), and others. These new types of FTAs typically include facilitation of foreign trade, liberalization and facilitation of foreign direct investment (FDI), and economic and technical cooperation, in addition to trade liberalization, which is included in traditional FTAs. It may be worth noting that the basic philosophy of these new types of FTAs is similar to that of Asia Pacific Economic Cooperation (APEC) forum, whose three pillars are (1) liberalization and (2) facilitation of foreign trade and foreign investment, and (3) economic and technical cooperation.

Many FTAs in East Asia are quite new and therefore their impacts may not have been fully materialized. However, a number of evidences on the impacts of FTAs in the form of trade expansion have been reported. For example, bilateral trade between China and Thailand has been reported to have increased notably after the enactment of an early harvest program under China-ASEAN FTA.

Although FTA may bring benefits in the form of trade expansion to FTA members, several possible negative impacts have been pointed out by researchers, business people, policy makers and others. First, some FTAs that are established in East Asia are of low quality in that a substantial number of commodities and/or important commodities are excluded from trade liberalization. Critics argue that because of low quality, FTAs will not generate expected trade expansion effect, but they only create distortions in the market. Second, proliferation of FTAs with different rules of origin is likely to give rise to the spaghetti bowl effect, which would reduce trade volume by creating impediments to trade. Third, an increased interest in FTAs is likely to have a negative impact on WTO negotiations by diverting interests and negotiating resources away from the WTO.

#### **IV.5. The Impacts of East Asia FTA: Simulation Results**

Given the emergence of FTAs in the region, it would be of interest to examine the possible impacts on FTAs on the East Asian countries. Ando and Urata (2006) analyzed the impacts of East Asia FTA by using a computable general equilibrium (CGE) model. Table 13 reports the macroeconomic effects of East Asia FTA on selected East Asian countries. The results show that all the East Asian countries will benefit from East Asia FTA, as all of them can expect an increase in both GDP and welfare.

In terms of GDP, East Asia FTA would increase overall GDP of East Asian countries by 1.5 percent. The impacts will be greater for the ASEAN countries when compared to the plus-three countries (China, Japan and Korea). Specifically, East Asia FTA will result in 6.4 percent increase of ASEAN's combined overall GDP, while the corresponding value for the plus-three countries is smaller at 0.93 percent. Wide variations are found for the impacts of East Asia FTA on GDP among the East Asian countries. The largest gain can be expected for Thailand, as its GDP is projected to increase by 15.4 percent. Other ASEAN countries can expect their GDP to increase by 5-6 percent, with the exception of Indonesia, whose GDP is projected to increase by 3.2 percent. Among the plus-three countries, Korea is expected to experience the largest increase in GDP by 4.9 percent, while China's and Japan's GDP are estimated to increase much less by 1.7 and 0.3 percent, respectively.

East Asia FTA would improve economic welfare for all East Asian countries. Wide variations in welfare gain per capita can be found among the countries but the ranking order of the countries in terms of welfare gain is found very different from the pattern observed for the increase in GDP growth. However, the ranking pattern becomes rather similar, if the increase in welfare per capita is compared to GNI (gross national income) per capita.

The impacts of East Asia FTA on its member countries largely depend on the initial level of import barriers and the importance of foreign trade in their economic activities, or trade-GDP ratios. We generally find the following relationship among the FTA member countries; the higher the level of import barriers, and/or the larger the trade-GDP ratios, the greater the gain from East Asia FTA.

Having discussed the wide variations in gains among the East Asia FTA member countries, it should be emphasized that all of them gain in terms of GDP as well as economic welfare.

While macroeconomic impacts of the East Asia FTA are positive, some sectors may suffer from the reduction in output, which in turn tend to result in the reduction in employment. This is because cheaper imports resulting from the East Asia FTA will substitute the domestic production. This substitution effect can be larger than the income effect, which would result from better resource allocation and would lead to the increase in demand for domestic production, resulting in the reduction in domestic production.

Table 14 shows the result of the model simulation on the sectoral impacts for the members of the East Asia FTA. ASEAN countries and Korea generally experience the increase in domestic production for most sectors because of the large increase in GDP. Some exceptions include Agriculture and food for Korea, transport equipment for Singapore and Vietnam, for which domestic production is projected to decline substantially. By contrast to these countries, China and Japan are projected to experience the decline of domestic production in several sectors, although the magnitudes of these declines are not so large.

We generally observe the sectoral impacts of East Asia FTA in such a pattern that the sectors with a comparative advantage would experience an increase (or a large increase) in production while the sectors with a comparative disadvantage would experience a reduction (or a small increase) in production.

## **V. Concluding Remarks**

This paper began with observing rapid expansion of foreign trade and foreign direct investment in East Asia, which played an important role in achieving successful economic development in the region. The subsequent analysis revealed the dramatic changes in trade patterns of East Asian economies in various aspects. First, intra-regional trade expanded faster than extra-regional trade, resulting in an increase in intra-regional dependency. Second, composition of trade shifted from non-manufacturing to manufacturing, especially to machinery products. Among machinery products, electronic and electric products increased their

importance. Third, trade in parts account for a large part of total trade (trade in parts and finished products) and the share is increasing. This pattern reflects increasing extent of division of labor inside East Asia as East Asia has become a factory for the world. Fourth, all these changes in trade patterns observed above appear to have resulted from active involvement of multinational corporations (MNCs) in foreign direct investment and foreign trade, as MNCs took an advantage of business opportunity arisen from freer trade and FDI environment, resulting from trade and FDI liberalization policies adopted by East Asian economies. Under liberalized market environment and efficient communications and transportations systems in recent years, MNCs fragmented production process into a number of sub-processes and then located the sub-processes in countries, where the sub-processes are undertaken most efficiently. As a result of fragmentation strategy by MNCs, regional production and distribution networks have been established in East Asia. These notable features of foreign trade in East Asian were generated by market forces. Focusing on increasing intra-regional trade, observers have described such development as market-driven regionalization.

However, market-driven regionalization seems to be giving way to institution-driven regionalization, as a number of attempts have been made to establish regional preferential agreements in the form of free trade agreement (FTA). An interesting and important question to be asked is whether FTAs would lead to further promotion of the trends and patterns realized so far and to achieve economic growth.

The impacts of FTA on trade among FTA members so far appear positive, being consistent with outcome projected by the simulation analysis using economic models. Many studies of the possible impacts of FTAs by using computable general equilibrium (CGE) models indicate positive impacts on trade and economic growth of the members. One would predict further development of the recent patterns of foreign trade in East Asia as FTAs lead to larger and freer trading environment inside the region.

Despite these positive impacts of FTAs, concerns have been raised about possible negative impacts, which may be caused by the proliferation of FTAs with different rules and contents. It is also important to emphasize the possible negative impacts on non-members.

Recognizing that global trade liberalization is optimum in terms of economic welfare for all the economies in the world, policy makers and researchers have to devise the scenario and policy to move from regional trade agreements such as FTAs to global trade liberalization. In this regard, it is important to make sure that existing and future FTAs are consistent with GATT/WTO rules, although these rules themselves have to be improved so as to successfully turn FTAs into global free trade.

1980=1

Figure 1 GDP, Exports, and FDI Inflows in East Asia (1980=199)

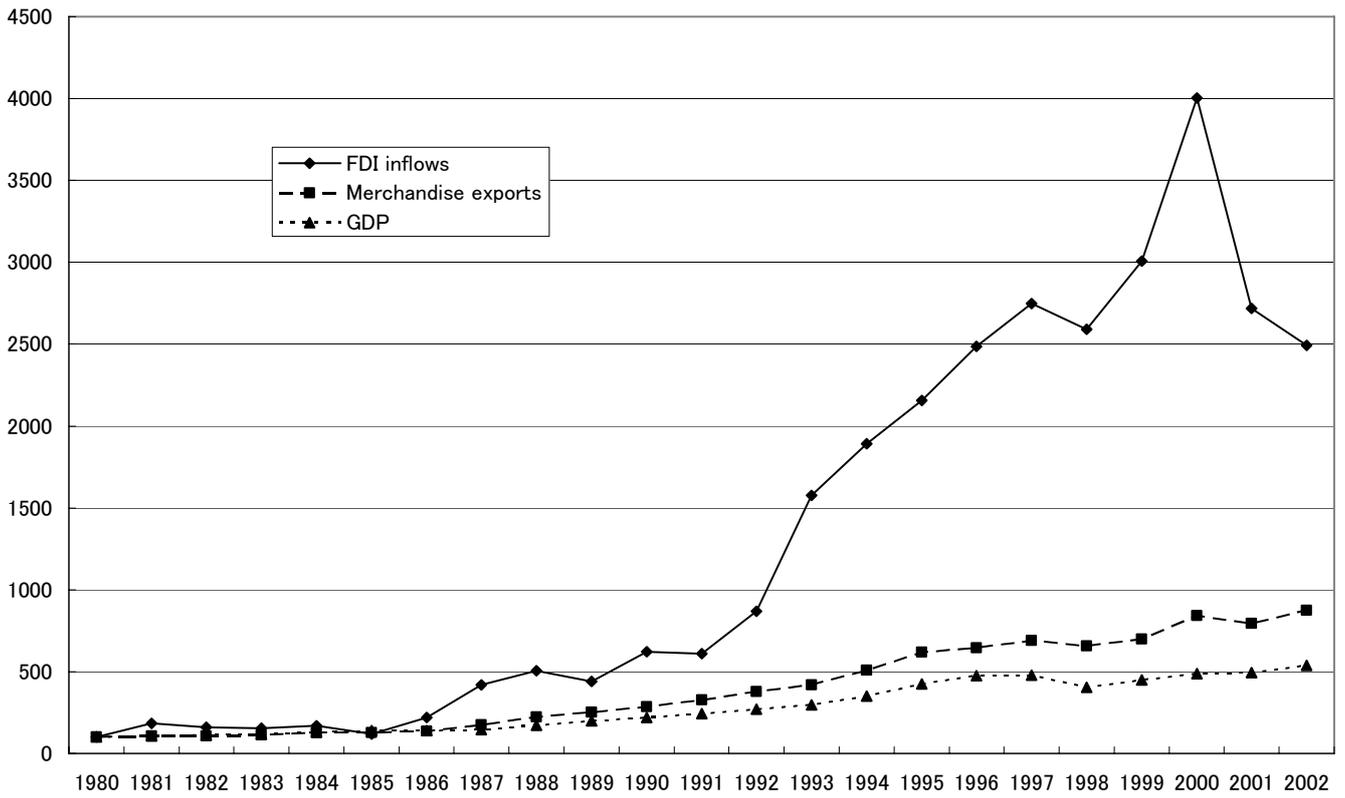


Figure 2 FDI Inflows to China, NIEs and ASEAN4: 3-year moving average

\$billion

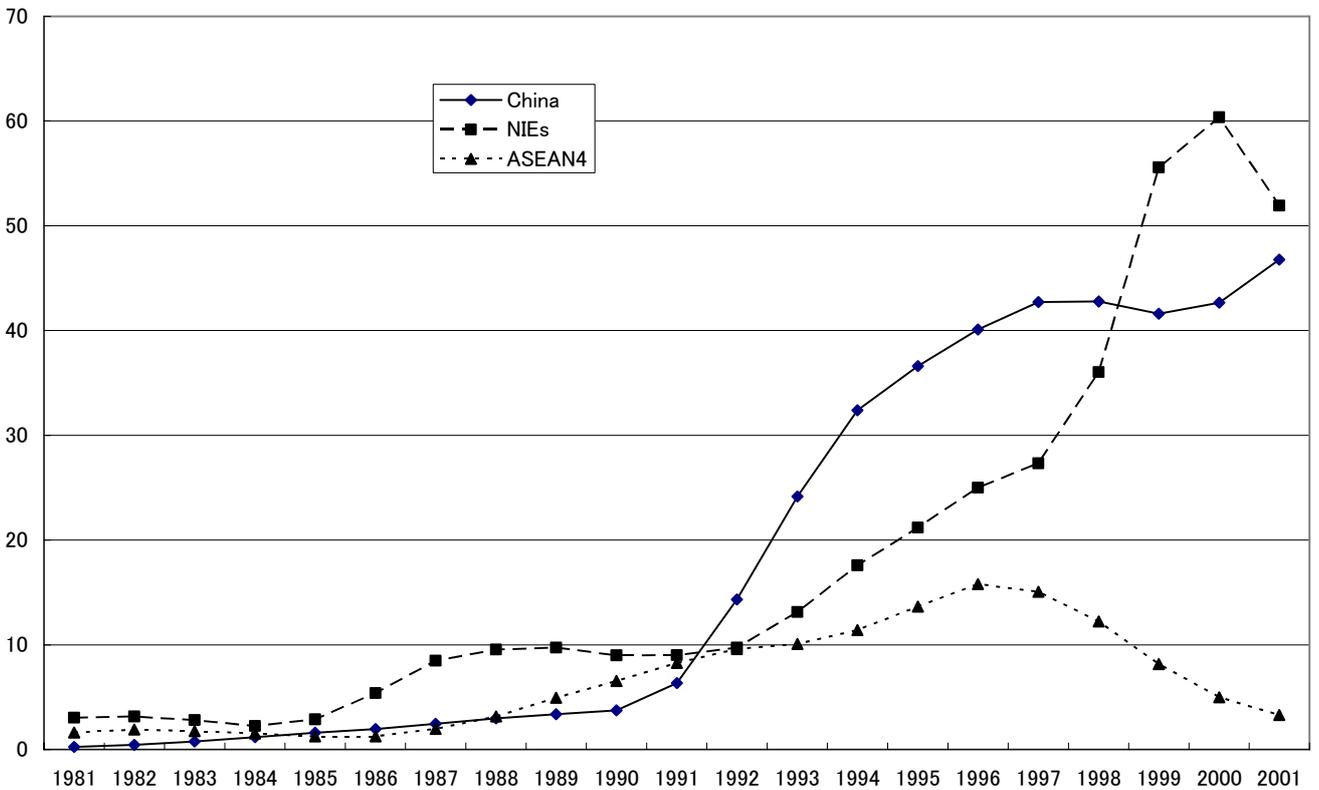


Table 1 GDP, Trade and Foreign Direct Investment for East Asia

	1980	1990	2000	2003	03/80 (ratio)
Value (\$billion)					
GDP	1,522.9	4,067.0	7,071.2	7,152.3	4.70
Exports	258.3	641.2	1,532.2	1,782.9	6.90
Imports	272.2	605.6	1,349.3	1,597.2	5.87
FDI Outflows	2.8	54.7	104.4	45.6	16.29
FDI Inflows	3.5	22.1	142.9	96.2	27.68
Share of world total (%)					
GDP	13.9	18.8	22.4	19.6	
Exports	12.8	18.3	23.5	23.5	
Imports	13.3	16.9	20.1	20.6	
FDI Outflows	5.2	22.6	8.8	7.5	
FDI Inflows	6.3	10.6	10.3	17.2	
Share of GDP (%)					
Exports	17.0	15.8	21.7	24.9	
Imports	17.9	14.9	19.1	22.3	
FDI Outflows	0.2	1.3	1.5	0.6	
FDI Inflows	0.2	0.5	2.0	1.3	
Excluding Japan					
Value (\$billion)					
GDP	460.2	1,027.3	2,325.1	2,851.4	6.20
Exports	127.9	353.6	1,052.9	1,311.0	10.25
Imports	130.9	370.2	969.8	1,214.2	9.28
FDI Outflows	0.4	6.7	72.8	16.8	40.40
FDI Inflows	3.2	20.3	134.6	89.9	28.10
Share of world total (%)					
GDP	4.2	4.7	7.4	7.8	
Exports	6.3	10.1	16.2	17.3	
Imports	6.4	10.3	14.5	15.7	
FDI Outflows	0.8	2.8	6.1	2.8	
FDI Inflows	5.8	9.7	9.7	16.1	
Share of GDP (%)					
Exports	27.8	34.4	45.3	46.0	
Imports	28.4	36.0	41.7	42.6	
FDI Outflows	0.1	0.6	3.1	0.6	
FDI Inflows	0.7	2.0	5.8	3.2	

Table 2 Foreign Trade of East Asian Countries

	1980	1990	2003	2003/ 1980	1980	1990	2003
	Exports (\$billion)			ratio	Exports/GDP (%)		
Japan	130.4	287.6	471.8	3.6	12.3	9.5	11.0
China	18.1	62.1	437.9	24.2	9.6	17.5	30.9
Hong Kong	20.3	82.4	228.7	11.3	71.1	109.2	145.9
Korea	17.5	65.0	193.8	11.1	27.4	24.6	32.0
Indonesia	21.9	25.7	61.0	2.8	28.1	22.4	29.3
Malaysia	13.0	29.5	99.4	7.7	52.0	66.9	95.8
Philippines	5.7	8.1	36.5	6.4	17.7	18.3	45.3
Singapore	19.4	52.7	144.1	7.4	165.4	142.9	157.8
Thailand	6.5	23.1	80.5	12.4	20.1	27.0	56.3
Brunei	4.6	2.2	4.4	0.9	na	na	na
Cambodia	0.0	0.1	1.7	105.6	na	7.7	40.0
Laos	0.0	0.1	0.4	13.5	na	9.1	17.8
Myanmar	0.5	0.3	2.6	5.5	na	na	na
Vietnam	0.3	2.4	20.2	59.7	na	37.1	51.5
	Imports (\$billion)			ratio	Imports/GDP (%)		
Japan	141.3	235.4	382.9	2.7	13.3	7.7	8.9
China	19.9	53.3	413.1	20.7	10.6	15.0	29.2
Hong Kong	23.0	84.7	233.2	10.1	80.5	112.3	148.8
Korea	22.3	69.8	178.8	8.0	34.9	26.5	29.5
Indonesia	10.8	21.8	32.6	3.0	13.9	19.1	15.6
Malaysia	10.8	29.3	81.9	7.6	43.4	66.5	79.0
Philippines	8.3	13.0	39.5	4.8	25.5	29.4	49.0
Singapore	24.0	60.8	127.9	5.3	204.9	164.7	140.1
Thailand	9.2	33.0	75.8	8.2	28.5	38.7	53.0
Brunei	0.6	1.0	1.7	3.0	na	na	na
Cambodia	0.2	0.2	1.7	9.5	na	14.7	40.6
Laos	0.1	0.2	0.5	5.7	na	21.4	24.7
Myanmar	0.4	0.3	2.6	7.4	na	na	na
Vietnam	1.3	2.8	24.9	18.9	na	42.5	63.5

Source: World Development Indicators 2005 CD-ROM

Table 3 Intra-regional Trade (%share of total)

	East Asia	NAFTA	EU
Exports			
1980	33.9	33.6	61.0
2003	49.4	55.4	61.4
Imports			
1980	34.8	32.6	56.9
2003	58.6	39.9	63.5

Source: JETRO trade database.

Table 4 Trade Composition: Shares in Total Trade (%)

	Manufactures				Electronic products			
	Exports		Imports		Exports		Imports	
	1980	2003	1980	2003	1980	2003	1980	2003
World	64.1	76.5	53.7	74.7	8.6	12.4	8.5	12.0
East Asia	na	na	na	na	20.5	30.0	10.5	23.7
Japan	94.7	93.1	18.7	57.6	23.3	19.1	4.8	14.2
Developing East Asia	na	na	na	na	18.6	33.6	13.6	26.5
China	na	90.6	na	80.0	5.0	26.9	7.6	23.3
Hong Kong	95.7	93.4	75.1	91.5	15.7	31.6	14.9	33.2
Korea	89.5	92.7	43.1	64.2	22.1	34.9	11.1	15.7
Taiwan	na	na	na	na	21.0	35.9	13.6	25.2
Indonesia	2.3	52.1	64.9	56.4	0.5	9.1	4.1	3.5
Malaysia	18.8	76.9	66.6	83.1	27.9	50.0	19.6	42.0
Philippines	21.1	90.1	47.5	79.5	22.4	67.9	15.7	34.2
Singapore	46.7	84.7	54.1	80.4	36.6	48.0	22.1	38.3
Thailand	25.2	75.4	50.8	75.9	15.3	24.2	10.4	19.5

Table 5 FDI Flows in East Asia

	1980	1990	2002	2002/ 1980	1980	1990	2002
FDI Outflows (\$million)				ratio	FDI Outflows / GDP		
Japan	2,385.0	48,024.0	28,800.3	12.1	0.2	1.6	0.7
China	0.0	830.0	1,800.0	na	0.0	0.2	0.1
Hong Kong	82.0	2,448.0	3,769.4	46.0	0.3	3.2	2.4
Korea	26.1	1,051.6	3,429.2	131.4	0.0	0.4	0.6
Indonesia	6.0	-11.0	130.2	21.7	0.0	0.0	0.1
Malaysia	201.1	129.0	1,369.5	6.8	0.8	0.3	1.3
Philippines	1.0	22.0	158.0	158.0	0.0	0.0	0.2
Singapore	97.6	2,033.8	5,536.2	56.7	0.8	5.5	6.1
Thailand	3.0	154.0	557.2	183.4	0.0	0.2	0.4
Brunei	0.0	0.0	4.6	na	na	na	na
Cambodia	0.0	0.0	9.7	na	na	0.0	0.2
Laos	0.0	0.0	76.0	na	na	na	na
Myanmar	0.0	0.0	0.0	na	na	0.0	0.0
Vietnam	0.0	0.0	0.0	na	na	na	na
FDI Inflows (\$million)					FDI Inflows / GDP		
Japan	278.0	1,753.0	6,324.3	22.7	0.0	0.1	0.1
China	57.0	3,487.1	53,505.0	938.7	0.0	1.0	3.8
Hong Kong	710.2	3,275.1	13,560.9	19.1	2.5	4.3	8.7
Korea	17.0	759.0	3,752.0	220.7	0.0	0.3	0.6
Indonesia	180.0	1,092.0	-597.0	-3.3	0.2	1.0	-0.3
Malaysia	933.9	2,611.0	2,474.0	2.6	3.7	5.9	2.4
Philippines	-106.0	550.0	319.0	-3.0	-0.3	1.2	0.4
Singapore	1,235.8	5,574.7	11,408.9	9.2	10.5	15.1	12.5
Thailand	189.4	2,575.0	1,802.0	9.5	0.6	3.0	1.3
Brunei	-19.6	3.0	2,009.0	-102.7	na	na	na
Cambodia	1.0	0.0	87.0	87.0	na	0.0	2.1
Laos	0.0	6.0	19.5	na	na	na	na
Myanmar	0.4	225.1	128.1	337.0	na	3.5	0.3
Vietnam	0.4	180.0	1,450.0	3696.9	na	na	na

Source: UNCTAD, FDI database, World Bank, World Development Indicators 2005 CD-ROM

Table 6 Sources of FDI Inflows to East Asian Developing Economies (%)

	China (actualized)		Indonesia (Approved)		Malaysia (Approved)		Philippines (BOP)		Singapore (committed)		Thailand (BOP)		Korea (Approved)		Taiwan (Approved)	
	1995-99	2000-04	1995-99	2000-04	1995-99	2000-04	1995-99	2000-04	1995-99	2000-04	1995-99	2000-04	1995-99	2000-04	1995-99	2000-04
World	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
East Asia	73.1	61.6	38.3	41.7	45.4	36.4	48.5	37.5	29.0	21.6	52.0	99.1	26.3	26.5	34.8	31.0
Japan	8.3	8.6	14.7	9.7	18.6	11.6	25.4	24.3	29.0	21.6	26.5	42.1	8.8	13.5	17.2	15.2
East Asia ex Japan	64.8	52.9	23.6	32.0	26.8	24.9	23.1	13.3	0.0	0.0	25.5	57.0	17.6	13.0	17.7	15.8
US	8.5	8.8	4.0	1.7	29.7	21.2	20.6	19.1	45.3	42.4	20.4	2.2	31.3	31.5	24.9	16.6
EU	7.7	7.0	24.0	17.0	9.1	30.3	18.7	4.8	23.2	30.8	17.3	-0.2	29.5	21.6	7.5	17.0

Note: The EU includes Italy, UK, the Netherlands, France and Germany. In the case of Singapore, the EU indicate

Source: Country data sources.

Table 7 Sectoral Distribution of FDI Inflows (%)

	Malaysia (Approved)		Thailand (BOP)		Korea (Approved)		Taiwan (Approved)	
	1995-99	2000-04	1995-99	2000-04	1995-99	2000-04	1995-99	2000-04
Manufacturing	100	100	100	100	100	100	100	100
Food	2.5	3.5	7.3	7.3	11.9	4.4	3.2	3.4
Textiles	2.6	1.9	4.2	2.6	1.3	0.9	2.8	1.3
Wood	8.2	8.0	a	a	11.3	0.9	0.5	1.6
Metals	8.3	9.6	20.2	13.6	3.6	5.1	12.2	6.9
Chemicals	33.0	17.1	9.3	10.2	18.9	18.5	12.6	10.0
General machinery	2.2	1.7	25.9	32.2	8.7	13.2	3.1	5.3
Electric machinery	35.4	43.1	26.9	11.9	29.6	35.9	56.9	61.9
Transport machinery	2.9	6.5	b	b	8.8	12.6	5.3	4.0
Others	4.9	8.4	10.9	22.3	5.5	8.4	3.4	5.5
Manufacturing share of total	na	na	39.6	53.5	49.4	36.4	48.6	35.0

Note: For Thailand Wood (a) is included in others and transport machinery (b) is included in general machinery.

Source: Country data sources

Table 8 Output sales and Input Procurement Patterns of Asian Affiliates of Japanese MNCs  
(Percent of total sales and total procurements)

	Sales			Procurement		
	Local Sales	Exports to		Local Procurements	Imports from	
		Japan	Asia		Japan	Asia
1992						
Manufacturing Total	66.1	15.8	11.2	48.5	37.9	8.9
Food	46.0	26.5	4.9	72.0	4.5	22.9
Textiles	56.1	14.2	12.3	40.7	22.4	12.1
Wood and Pulp	50.2	47.2	0.3	83.7	13.2	0.3
Chemical Products	64.7	4.9	28.6	71.4	16.9	3.5
Iron and Steel	85.5	2.1	8.6	29.0	47.3	22.3
Non-ferrous Metal Products	63.3	21.4	14.9	64.8	9.2	6.2
General Machinery	53.0	23.6	11.3	49.0	47.8	1.1
Electric Machinery	45.7	27.2	19.0	36.6	46.7	15.4
Transport Machinery	92.6	1.7	1.0	52.9	43.8	1.1
Precision Instruments	36.9	51.8	1.9	34.2	60.2	3.7
Coal and Petroleum Products	55.9	0.0	0.2	92.6	3.8	2.5
Other Manufacturing	78.6	9.4	5.6	58.6	27.5	6.2
2001						
Manufacturing Total	47.9	24.6	18.3	43.9	36.1	17.4
Food	80.2	7.6	8.9	73.6	8.7	11.8
Textiles	40.3	35.3	14.5	58.5	25.0	6.9
Wood and Pulp	81.7	13.2	2.8	90.0	6.2	2.2
Chemical Products	65.3	8.9	21.7	60.3	17.1	16.1
Coal and Petroleum Products	26.8	52.1	17.9	35.9	2.7	56.1
Iron and Steel	85.7	1.9	10.1	27.1	63.2	8.7
Nonmetallic Products	53.7	17.3	25.8	64.2	19.0	11.3
General Machinery	34.9	40.2	17.1	59.1	36.2	4.3
Electric Machinery	34.5	28.0	16.9	41.1	32.7	25.3
IT Machinery	30.1	36.9	23.6	31.5	37.0	29.7
Transport Machinery	66.1	8.1	16.4	47.4	46.4	3.9
Precision Instruments	42.3	40.3	12.9	50.9	41.5	7.4
Other Manufacturing	49.9	31.4	9.8	43.9	40.8	12.4

Source: Ministry of Economy, Trade and Industry, Kaigai Jigyo Katsudo Kihon Chosa (Comprehensive Survey of Overseas Activities of Japanese Firms), No. 23, 1994 and No. 32, 200

Table 9 Intra-firm Transactions for Asian Affiliates of Japanese MNCs  
(Percentage share of Transaction)

	Sales			Procurement		
	Local Sales	Exports to		Local Procurements	Imports from	
		Japan	Asia		Japan	Asia
1992						
Manufacturing Total	6.3	84.2	44.4	4.2	78.0	50.2
Food	7.6	85.4	26.3	0.2	75.8	48.8
Textiles	4.3	36.1	23.0	19.5	34.2	31.5
Wood and Pulp	0.0	57.9	0.0	0.1	79.4	0.0
Chemical Products	2.4	49.0	3.2	18.0	57.5	4.3
Iron and Steel	0.0	29.0	0.0	5.2	1.1	0.0
Nonmetallic Products	0.8	82.6	55.1	0.0	26.0	0.0
General Machinery	3.0	96.7	55.6	4.5	93.9	84.8
Electric Machinery	8.0	90.0	53.7	2.0	84.6	59.8
Transport Machinery	7.2	73.9	57.9	0.6	81.7	34.6
Precision Instruments	32.4	96.5	77.9	17.5	85.6	100.0
Coal and Petroleum Products	0.0	0.0	0.0	0.0	100.0	10.0
Other Manufacturing	6.3	67.0	49.8	7.3	64.1	61.8
2001						
Manufacturing Total	49.6	96.0	70.2	86.0	46.7	65.9
Food	48.9	78.7	66.6	98.4	52.3	24.2
Textiles	28.5	89.8	59.1	89.7	52.2	85.2
Wood and Pulp	26.3	82.8	100.0	98.8	100.0	100.0
Chemical Products	41.2	77.1	50.5	96.7	74.6	87.4
Coal and Petroleum Products	88.9	100.0	99.4	100.0	0.0	78.9
Iron and Steel	8.0	86.6	27.9	86.4	81.9	100.0
Nonmetallic Products	19.5	97.8	65.4	66.3	54.7	87.8
General Machinery	61.8	98.7	91.8	84.7	59.1	61.6
Electric Machinery	45.0	98.3	75.8	89.3	27.7	29.8
IT Machinery	56.9	95.5	80.8	89.8	44.3	72.6
Transport Machinery	56.4	99.5	29.8	73.7	46.4	83.4
Precision Instruments	58.7	99.5	93.7	96.6	50.9	89.2
Other Manufacturing	56.5	98.4	78.2	92.1	29.4	77.9

Source: Ministry of Economy, Trade and Industry, Kaigai Jigyo Katsudo Kihon Chosa  
(Comprehensive Survey of Overseas Activities of Japanese Firms), No. 23, 1994 and No. 32, 2004.

Table 10 Proportions of Electronics Components Trade in Total Electronics Trade: 2002

	Exports					Imports				
	East	Japan		EU	World	East	Japan		EU	World
China	0.65	0.49	0.29	0.32	0.48	0.77	0.80	0.57	0.58	0.74
Hong Kong	0.78	0.57	0.44	0.47	0.67	0.71	0.75	0.66	0.50	0.70
Korea	0.71	0.74	0.42	0.43	0.57	0.81	0.74	0.66	0.62	0.73
Taiwan	0.85	0.62	0.49	0.50	0.66	0.78	0.71	0.70	0.68	0.74
Indonesia	0.77	0.50	0.37	0.16	0.52	0.79	0.88	0.48	0.37	0.73
Malaysia	0.86	0.57	0.40	0.59	0.65	0.87	0.88	0.84	0.82	0.86
Philippines	0.88	0.66	0.63	0.73	0.76	0.82	0.89	0.94	0.79	0.87
Singapore	0.80	0.69	0.52	0.55	0.67	0.82	0.81	0.69	0.74	0.79
Thailand	0.91	0.69	0.46	0.56	0.68	0.81	0.81	0.78	0.49	0.76
East Asia	0.78	0.61	0.43	0.48	0.62	0.78	0.79	0.72	0.64	0.76
Japan	0.79	---	0.42	0.43	0.61	0.61	---	0.48	0.50	0.57
NAFTA	0.72	0.48	0.45	0.48	0.52	0.43	0.42	0.45	0.49	0.44
EU	0.64	0.50	0.49	0.41	0.44	0.48	0.43	0.48	0.41	0.43
World	0.76	0.57	0.44	0.43	0.54	0.62	0.61	0.52	0.44	0.54

Source: Computed from ITI (Institute of International Trade and Investment) trade database.

Table 11 Trade Liberalization in Selected East Asian Economies

		All products			Primary products		Manufactured products		Ad valorem equivalent of non-tariff barriers
		Binding Coverage	Unweighted averages	Import-weighted averages	Unweighted averages	Import-weighted averages	Unweighted averages	Import-weighted averages	
China	1992		40.4	32.1	36.1	14.1	40.6	35.6	
	2004	100	9.8	6.0	10.0	5.6	9.7	6.0	1.5
Indonesia	1989		19.2	13.0	18.2	5.9	19.2	15.1	
	2003	96.6	6.4	5.2	8.0	3.1	6.1	5.8	0.5
Japan	1988		4.2	3.6	8.3	4.4	3.5	2.7	
	2004	99.6	2.9	2.4	5.3	3.9	2.4	1.6	1.6
Korea	1988		18.6	14.0	19.3	8.3	18.6	17.0	
	2002	94.4	15.5	9.5	20.9	19.0	7.8	5.0	0.0
Malaysia	1988		14.5	9.7	10.9	4.6	14.9	10.8	
	2003	83.7	7.3	4.2	4.5	2.1	7.8	4.6	1.7
Philippines	1988		28.3	22.4	29.9	18.5	27.9	23.4	
	2003	66.8	4.5	2.6	5.7	5.0	4.2	2.0	0.4
Singapore	1989		0.4	1.1	0.2	2.5	0.4	0.6	
	2003	69.8	0.0	0.0	0.0	0.0	0.0	0.0	0.5
Thailand	1989		38.5	33.0	30.0	24.3	39.0	35.0	
	2003	75.0	14.0	8.3	16.4	4.4	13.5	9.3	0.3
Vietnam	1994		14.8	20.6	20.9	46.7	13.9	13.1	
	2004		13.7	13.7	18.1	16.7	12.9	12.5	
India	1990		79.0	56.1	69.8	34.1	79.9	70.8	
	2004	73.8	28.3	28.0	30.0	36.9	27.9	25.3	3.2

Source: World Bank, World Development Indicators 2005

Table 12 Major FTAs Involving East Asian Economies (as of April 2006)

In Action	In Negotiation	Under Study
Bangkok Treaty (1976)	China-Thailand*	China-India
AFTA(1992)	China-Australia	Japan-Australia
Singapore-New Zealand (2001)	China-New Zealand	Japan-India
Japan-Singapore (2002)	China-Chile	Korea-ASEAN
Singapore-Australia (2003)	Japan-ASEAN	Korea-Australia
Singapore-EFTA (2003)	Japan-Indonesia	Korea-New Zealand
Singapore-US (2004)	Japan-Korea	Korea-Thailand
Korea-Chile (2004)	Japan-Malaysia*	Korea-US
China-Hong Kong (2004)	Japan-Thailand	ASEAN-India
China-Macau (2004)	Japan-Philippines	ASEAN-US
Taiwan-Panama(2004)	Korea-ASEAN	ASEAN-CER
Japan-Mexico (2005)	Korea-Singapore*	Malaysia-EU
Thailand-Australia (2005)	Malaysia-Australia	Malaysia-India
Thailand-New Zealand (2005)	Malaysia-New Zealand	Philippines-US
China-ASEAN(2005)	Singapore-Canada	Singapore-Chile
India-ASEAN(2005)	Singapore-Mexico	Singapore-Taiwan
India-Sri Lanka	Singapore-India*	India-GCC
	Singapore-Sri Lanka	India-Malaysia
	Singapore-Qatar*	
	Singapore-Peru	
	Singapore-Panama	
	Singapore-Kuwait	
	Singapore-Brunei-Chile-NZ	
	Thailand-India*	
	Thailand-US	
	Thailand-Peru*	
	Thailand-EFTA	
	Hong Kong-New Zealand	
	India-Mauritius	
	India-Chile	
	India-Egypt	

Note: '\*' indicates conclusion of the negotiation.

Source: Country sources

Table 13 Effects of EAFTA on East Asian Countries

	Increase in GDP (%)	Increase in Welfare (\$million)	Increase in Per capita welfare \$(1)	Per capita GNI (\$) (2)	(1)/(2)(%)
China	1.73	14,483	11	900	1.22
Japan	0.31	15,013	118	35,780	0.33
Korea	4.91	17,122	360	10,580	3.40
Indonesia	3.22	4,663	22	680	3.24
Malaysia	5.64	4,900	207	3,410	6.07
Philippines	5.06	2,707	34	1,030	3.30
Singapore	5.17	4,805	1,443	21,440	6.73
Thailand	15.37	14,420	230	1,980	11.62
Vietnam	6.05	4,976	34	410	8.29
CJK(+3)	0.93	46,619	32		
ASEAN	6.39	36,471	69		
ASEAN+3	1.48	83,090	42		

Source: Simulation results.

Per capita GNI are taken from World Bank, WDI-CD-ROM

Table 14 Effects of East Asia FTA on output in East Asian Countries

(Changes in volume in millions US\$, %)

	Japan	China	Korea	ASEAN	Indonesia	Malaysia	Philippines	Singapore	Thailand	Vietnam
Agriculture and food	-2.0	5.5	-13.0	5.7	2.7	6.9	1.9	51.1	11.4	1.0
Natural resources	-0.1	0.1	-0.7	1.8	1.1	1.5	1.5	1.2	4.6	3.0
Textile and apparel	2.8	0.2	33.6	7.4	3.3	18.9	9.1	-3.2	7.5	10.4
Wood and paper products	-0.4	-1.6	5.7	8.3	7.7	6.1	5.1	4.4	11.2	14.9
Chemical products	1.3	-1.3	8.0	12.0	5.5	8.9	6.4	9.7	23.7	16.4
Metal products	2.2	-1.3	3.4	8.4	2.6	8.3	7.6	6.8	21.3	2.9
Machinery	2.6	-1.6	1.5	20.0	12.8	17.0	19.9	14.6	33.8	14.6
Electronic machinery	-2.1	11.5	4.0	10.0	7.4	5.2	7.7	7.6	34.0	0.6
Transport equipment	1.5	-3.7	1.0	0.1	-0.6	4.6	32.5	-11.6	14.7	-23.1
Other manufacturing	-1.6	-0.3	35.9	8.8	-2.0	8.4	4.7	-0.1	11.3	17.6
Trade	0.2	0.6	5.1	6.6	3.8	2.3	5.7	3.3	16.2	6.1
Construction	0.6	3.7	7.2	9.3	4.9	6.7	7.1	8.2	22.4	9.1
Transport and communication	0.1	0.7	1.5	4.7	3.3	3.1	4.8	0.8	9.9	7.1
Public services	0.1	0.8	1.7	2.7	1.2	2.5	1.9	4.0	4.8	1.2
Other services	0.2	0.7	3.9	4.8	2.7	2.1	4.9	0.5	13.3	5.5

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
FDI inflows	100	185.68	161.07	155.87	168.24	120.15	220.5	420.51	504.6	440.68	622.33	610.8	867.62	1575.3	1890.8	2156.7	2486.2	2748.6	2591.5	3008	4004.4	2718.7	2492.1
Merchandise exports	100	108.34	107.85	112.17	128.72	127.56	136.98	176.75	224.14	251.37	284.49	328.23	376.77	420.71	508.33	619.73	645.61	691.01	658.55	698.57	841.67	793.04	873.27
GDP	100	108.05	113.3	119.03	129.49	139.54	140.18	145.08	173.44	199.74	219.76	244.93	272.1	296.18	350.87	424.85	475.03	478.23	404.58	448.61	488.08	494.49	537.33

Source: GDP, exports (World Bank World Development Indicators 2005 CD-ROM), FDI (UNCTAD FDI database)

FDI inflows (3-year moving average) \$billion

	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
China	0.2507	0.4437	0.7747	1.1843	1.5973	1.9493	2.461	2.967	3.358	3.7487	6.3363	14.346	24.153	32.384	36.605	40.089	42.723	42.769	41.614	42.646	46.773
NIEs	3.0351	3.161	2.802	2.2498	2.8793	5.3855	8.4701	9.5586	9.7422	8.9922	9.0087	9.7263	13.127	17.578	21.188	24.999	27.313	36.024	55.564	60.353	51.922
ASEAN4	1.6292	1.9018	1.7594	1.5439	1.2511	1.261	1.9799	3.1647	4.9519	6.5496	8.2667	9.587	10.093	11.415	13.635	15.799	15.053	12.226	8.1553	4.9898	3.2877

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### **3. Economic Integration in East Asia: A Financial and Monetary Perspective**

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#### **1. Introduction**

Since the 1990s, the economies of East Asia have been increasingly integrated due to active private sector initiatives, as evidenced by an expansion of bilateral trade, FDI, other financial flows, and by tourism. Intra-regional trade has reached more than 50 percent of total trade. Such linkages are likely to strengthen further thanks to the prevalence of regional preferential trade arrangements initiated since the late 1990s. Like other Asian countries (e.g., China, Singapore, and Thailand), Japan has pursued negotiating regional preferential arrangements—mainly in the form of EPAs (Economic Partnership Arrangements) covering a wider range of issues (such as the free flow of goods, money and labor) rather than FTAs (Free Trade Arrangements). EPAs have already been implemented with Singapore (2002) and Mexico (2005). An agreement was signed with Malaysia in 2005, and agreements in principle on major elements were reached with the Philippines in 2004 and Thailand in 2005. Currently, negotiations are underway with Indonesia, Brunei, Korea, Chile, and ASEAN as a group.

To date, all the preferential arrangements in East Asia are solely based on bilateral or sub-regional levels, but do not extend to a regional scale. The proliferation of overlapping preferential agreements tends to intensify the administrative burden and inefficiencies among the signing countries, due to different schedules for phasing out tariffs and non-tariff barriers, local content requirements, coverage of excluded items, investment rules, etc.; the so-called “spaghetti bowl” effect as pointed out by Prof. Jagdish Bhagwati of Colombia University. Therefore, for reasons relating to efficiency, it is clear that region-wide preferential arrangements are superior to the existing EPAs and FTAs. Nonetheless, progress toward such a movement is barely noticeable.

Instead of regional-wide trade arrangements, movements towards regional financial and monetary cooperation have made some progress, particularly in the aftermath of the East Asian financial crisis of 1997-98. Three strong and increasingly prevalent views have promoted these post-crisis movements. One is that a regional emergency financial support mechanism is necessary as a “crisis management” measure, given that the timing of International Monetary Fund (IMF) disbursements is often slow and its usable resources occasionally suffer from shortages. Such a regional support mechanism is feasible in East Asia because of the high level of savings and substantial amounts of foreign reserves. The second view is that more balanced financial and capital markets should be developed as a “crisis prevention” measure. Prior to the crisis, Asian banks appeared to not function properly due to cronyism (among banks, firms and governments), an inability to develop risk management skills and a lack of proper prudential risk management. The crisis underscored the risks associated with financial structures where firms depended excessively on short-term bank loans to finance longer-term domestic projects, while using non-hedged short-term foreign currency borrowings to finance domestic investment projects.<sup>1</sup> Thus, reducing these

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<sup>1</sup> The East Asian crisis was essentially the external debt problems existing between financial institutions in both lending and borrowing countries. By contrast, crises in other emerging market economies—such as Russia (1998), Brazil (1999), and Argentina (2001-03)—were associated with external debt problems between sovereign borrowers and overseas private investors. Both crises were preceded by the growth of capital inflows and

mismatches by developing more balanced financial and capital markets is crucial to prevent a new type of crisis emerging in East Asia. The third view is that flexible exchange rate regimes are more suitable for economies with open capital accounts, and might even function as a “crisis prevention” measure. This reflects the observation that crisis-affected countries had adopted a de facto dollar peg prior to the crisis, but were forced to abandon it and adopt a flexible exchange rate regime in the event of a reversal of massive capital flows and the resultant depletion of foreign reserves. However, regional currency cooperation is regarded as superior to individually adopted flexible exchange rate regimes, as it reduces exchange rate volatility and thus encourages further private sector activities.

The growing volumes of capital flows, volatility, and swings in investor risk sentiment increasingly create turbulence in international markets. This trend might increase the likelihood of contagious crises, like the East Asian crisis of 1997-98, especially since rapid intra-regional private sector activities have strengthened trade and investment linkages in the region. Thus, it is becoming important for East Asia to consider measures to prevent or mitigate crises so as to sustain stable and prosperous economies in the region. The approach sought by East Asia—namely, a strategy that proceeds with financial and currency cooperation—would differ from that of Europe, where trade integration took place in the 1950s prior to monetary and currency cooperation.<sup>2</sup> In Europe, discussion about currency and financial coordination did not take place until the emergence of speculative currency attacks in the late 1960s and the collapse of the Bretton Woods system in the early 1970s, because the system maintained global exchange rate stability. Also, moderate capital controls that had continued until the Single European Act of 1987 did not promote financial coordination in the initial stage. This chapter critically reviews measures that have been extensively discussed and are implemented in East Asia, as well as the issues remaining on the agenda.

## **2. Mechanism of the East Asian Crisis and Policy Response**

### **2-1. Nature of the Crisis**

The East Asian crisis erupted in a new environment where massive international capital, largely in the form of short-term capital, shifted from advanced countries (i.e., Japan, the US, and the EU) to the emerging-market economies in East Asia. The capital inflows took place after East Asian governments in the early 1990s had liberalized their domestic financial sectors (through interest rate decontrol and entry deregulation) as well as their capital accounts. Massive capital inflows to the region reflected strong macroeconomic fundamentals, interest rate differentials and limited exchange rate risk guaranteed under fixed exchange rate regimes. Until the crisis occurred, the region’s economic performance had been remarkable: an average economic growth of 7 percent with an export orientation, a high level of savings (about 30 percent of GDP) and a fiscal surplus. Reflecting active private sector investment activities and high demand for credit, domestic interest rates had been higher than those in advanced countries.

The amount of capital inflows surpassed the amount needed to finance the underlying international current account deficits, thus giving rise to a surplus in the overall balance of payments and an increase in

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triggered by a reversal of capital flows caused by a change in investor sentiment. Nevertheless, conflicts of interests among creditors, and between creditors and borrowers, were more complicated in Russia, Brazil, and Argentina than those in East Asia, since the presence of a large number of individual investors in the former made it difficult to agree on how to restructure sovereign foreign debt. While major borrowers were largely domestic financial institutions and firms, and major lenders were foreign banks in East Asia, the major borrowers were sovereign and the major lenders were a large number of individual investors in the other regions.

<sup>2</sup> The European Payments Union was operated between 1950 and 1958. However, intense discussion over currency and financial coordination did not take place at that time. In 1979, the European Monetary System was introduced with the European Currency Unit and Exchange Rate Mechanism.

foreign reserves. The increase in foreign reserves generated excessive liquidity (as a result of intervention in the foreign exchange market by the authorities to maintain the dollar peg) and a credit expansion by domestic financial institutions resulted, thereby giving rise to excessive borrowing by domestic firms. This led to an expansion of domestic expenditure (or absorption) and thus a widening of the international current account deficit. The growth in domestic credit amplified the boom-bust business cycle in real estate and stock prices as well as in the accumulation of production capacity, which increased the vulnerability of domestic financial institutions and firms by enlarging potential losses arising from a possible burst of the bubble and the excess production capacity. Massive, short-term and foreign currency-denominated borrowing by domestic financial institutions (and longer-term, domestic currency-denominated lending by them) aggravated maturity and currency mismatches (double mismatches). Maturity mismatches widened because domestic financial institutions borrowed short and invested in longer-term real estate and in production capacity in the manufacturing sector without carefully examining the creditworthiness of the domestic borrowing firms. A currency mismatch also grew as domestic financial institutions increased foreign currency-denominated loans and provided domestic currency-denominated loans to the domestic sector without adequately hedging the exchange rate risk. The belief that the dollar peg would be sustained supported this trend.

Excess capital formation and the burst of the bubble, which had become prevalent in 1995-96, caused the deterioration of the credit quality of domestic financial institutions and thus their balance sheets by increasing the size of non-performing assets. Triggered by this and a slowdown in economic growth, the trends in capital flows started to reverse as investor sentiment toward East Asia deteriorated. Subsequently, sudden and massive capital outflows followed, leading to a deficit in the overall balance of payments. A drain in foreign reserves left Thailand no choice but to abandon the dollar peg in July 1997. Thai economic performance deteriorated sharply due to mutually reinforcing currency and banking crises (so-called “twin crises”). The presence of the afore-mentioned double mismatches significantly deepened the twin crises, since the sharp depreciation of the exchange rates swelled the domestic currency value of foreign-denominated liability in addition to the increase in non-performing assets. The banking sector problems brought on a credit crunch, making it harder for domestic firms to get new borrowing and this led to an abrupt curtailment of domestic expenditure. The Thai crisis triggered speculative currency attacks on neighboring East Asian countries, in the same year generating damaging effects particularly on Indonesia and Korea (Table 1). The East Asian crisis also generated contagious effects in Russia in 1998, Brazil in 1999, and Argentina in 2001-03 as well as globally in various other emerging market economies.

The East Asian crisis was essentially a “capital account” crisis triggered by flows of massive foreign capital. Financial sector and capital account liberalization in the early 1990s promoted reckless lending by domestic financial institutions, since the new environment caused by deregulation was not accompanied by the necessary prudential and regulatory framework. The nature of the capital account crisis differs substantially from that of a conventional crisis (a so-called a “current account” crisis) that generally arises from poor macroeconomic performance (i.e. low economic growth, a low level of savings, fiscal deficit financed by money creation and external debt, and high inflation). For a country subject to a current account crisis, a low level of savings and a fiscal deficit financed by monetization generates a large international current account deficit that exceeds capital inflows, causing a deficit in the overall balance of payments (and a drain in foreign reserves) and so leads to a crisis. Thus, a current account crisis is triggered by poor macroeconomic performance, whereas a capital account crisis is triggered by changes in investor sentiment and a reversal of capital flows.

**Table 1. Economic Performances of Thailand, Indonesia, and Korea**

	1996	1997	1998
<b>Real GDP Growth (%)</b>			
Thailand	5.9	-1.4	-10.5
Indonesia	7.6	4.7	-13.1
Korea	7.0	4.7	-6.9
<b>Exchange Rate (to 1US\$)</b>			
Thailand	25.6	47.2	36.7
Indonesia	2383	4650	8025
Korea	844	1695	1204

**Source: IMF, International Financial Statistics.**

## 2-2. IMF Response to the Crisis

As economic conditions deteriorated sharply and the need for foreign currencies intensified, at end-July 1997 Thailand requested assistance from the IMF. This move was followed by Indonesia in October and Korea at end-November in the same year. In response, the IMF provided rescue packages (financial loans together with policy programs as conditionality) in cooperation with the World Bank, the Asian Development Bank and bilateral contributors. The rescue packages amounted to US\$17.2 billion for Thailand, US\$23 billion plus a second line of defense for Indonesia, and US\$35.2 billion plus a second line of defense for Korea. IMF loans are generally accompanied by programs of policies to increase the probability of repayment to the IMF and, at the same time, promote an incentive for recipient countries to undertake better macroeconomic policies. For this reason, IMF loans are phased, and disbursements are made based on the performance of the agreed programs.

The announced IMF-led financial packages for East Asia were greater than the size usually provided by the IMF, but in this they revealed some problems. First, the IMF's financial assistance is phased so that the announced amount of loans cannot be disbursed all at once. Also, governments need to reach an agreement over the programs of policies with the IMF prior to the disbursement, thus it is difficult for the IMF to provide immediate loans. The slow and phased style of disbursement may be appropriate for a conventional current account crisis, but not for a capital account crisis. Second, the second lines of defenses announced by some bilateral creditors (e.g., the US and Japan) were never meant to be disbursed in the cases of Indonesia and Korea. Thus, the amounts of actually available financial resources were smaller than those announced. Third, the IMF-supported programs of policies covered changes in the exchange rate regimes, a tightening of monetary and fiscal policies, and a wide range of structural reforms. The phased, conditional and restrictive bailout lending was criticized by many academics (e.g. Radelet and Sachs [1998], Rose [1998]), who claimed that external assistance did not arrive quickly or massively enough to prevent credit crunches and recessions, and, further, did not successfully prevent investor panic from deepening in East Asia.

Moreover, the East Asian crisis and subsequent contagious crises awakened the world to the fact that the IMF's financial resources might not be sufficient to cope with a large number of crises. The IMF could act as a crisis lender for member countries through utilizing fund-raising mechanisms—such as the General Arrangements to Borrow (GAB), New Arrangements to Borrow (NAB), and participation by other member countries and international financial institutions—as well as the issue of Special Drawing Rights

(SDRs). The amount of total IMF's resources (holding of gold and currencies) was US\$283 billion in April 2001. Once non-usable resources and committed usable resources are excluded from this total amount, usable resources were just US\$99 billion. Adding in the resources available under GAB and NAB, total usable resources were up to US\$145 billion. If a series of greater massive contagious crises had occurred globally at that time, this amount might not have been sufficient. Academics (such as Rogoff [1999]) stressed that the IMF's resources might not be sufficient to preclude a broad-based attack on emerging market economies.

In response to some of the criticisms, the IMF invented new financial arrangements so that crisis-affected countries could get a relatively large amount of disbursement from the IMF. Typically, the maximum amount of financial resources available to member countries is determined based on the size of quota applicable to each. In December 1997, the IMF introduced the Supplementary Reserve Facility (SRF), which aims to provide financial support for one year without any general access limits to a country suffering serious balance of payments problems caused by a sudden and destructive loss in market confidence, with repayment due up to 1.5 years later. The SRF is applicable to countries that could recover in a relatively short term from a crisis once sufficient foreign exchange is provided and appropriate economic policies are implemented. The SRF is tied to the existing Stand-By Facility and is a conditional lending facility. The interest rate is a rate of the normal charge plus 300 basis points for the first year and plus an additional 50 basis points for each six months thereafter with a maximum charge of 500 basis points. Indeed, SRFs were applied to Korea, Brazil and Argentina.

As a preemptive measure to prevent a crisis, the IMF in addition introduced the Contingent Credit Line (CCL) in April 1999. The CCL is applicable to a country threatened with potential vulnerability to contagion, but is not yet facing a crisis, while the SRF is used for a country already in crisis. The availability of CCL is up to 300 to 500 percent beyond the quota. The interest rate is the rate of a normal charge plus 150 basis points for the first year plus an additional 50 basis points for each six months thereafter with a maximum charge of 350 basis points. The CCL is tied to ongoing performance criteria, such as good performance under annual IMF consultations or under a program, adherence to international standards and maintenance of constructive relations with private creditors, etc. These criteria were criticized for not being clearly defined, which could raise concerns regarding transparency. The CCL was abolished in November 2003 without receiving any application from a member country. The failure of its activation reflected the situation that a country did not have an incentive to apply for fear of concern that the application itself would be interpreted by investors as a sign of weakness and thus precipitate the very crisis that the arrangement wanted to prevent.

### **3. Movements Toward Regional Financial Arrangements**

#### **3-1. Asian Monetary Fund Proposal**

The vision for establishing the Asian Monetary Fund (AMF) was formed in August 1997, when Japan proposed the idea with several member countries of the ASEAN at a meeting in Tokyo held to plan financial support for Thailand. The proposal emerged in response to a request by Thailand to create a scheme that would enable urgent financing for crisis-affected East Asian countries. The AMF was positioned to be independent of the IMF. In September 1997, Japan officially announced a plan to establish the AMF in cooperation with other Asian countries to stabilize Asian currencies and financial markets. Initially, the AMF aimed to raise US\$50-60 billion through contributions from participating countries and another US\$50 billion through the contribution of Japan. It was envisioned to initiate within 1997—with possible initial

membership from the ASEAN-6 (Brunei, Indonesia, Malaysia, the Philippines, Singapore, and Thailand), Korea, China, Taiwan and Hong Kong—and make up for IMF regional surveillance activities. The AMF vision was to achieve financial cooperation on a regional multilateral basis in East Asia.

However, the AMF proposal met strong opposition from the US and IMF on the grounds that such an arrangement would enhance the problems of moral hazard and double standards (two layers of conditionality imposed separately by the IMF and AMF), and that any challenge to the IMF leadership would be undesirable. Accordingly, Japan decided to give up the proposal in November 1997. Instead, the Group of 15 economies met in Malaysia and developed a plan to prevent renewed currency and financial market turbulence. In preparation for an APEC summit meeting, senior finance officials of APEC member countries met in Manila in mid-November 1997 to design a framework for dealing with crises in the region. This “Manila Framework” was endorsed by the 18 leaders of the APEC economies at the forum's annual summit at end-November 1997. The Framework recognized that the role of the IMF would remain central and stressed enhanced regional surveillance through intensified economic and technical cooperation. In December 1997, ASEAN endorsed the Manila Framework and decided to develop a regional surveillance mechanism that would emphasize preventive efforts to avoid financial crises, and reaffirmed their commitment to maintain an open trade and investment environment in the ASEAN area.

In October 1998, Japan proposed a framework called “A New Initiative to Overcome the Asian Currency Crisis” (the so-called “New Miyazawa Initiative”). The initiative was to provide financial support measures totaling US\$30 billion. Of the total amount, US\$15 billion would be made available for medium- to long-term financial needs for East Asian countries and another US\$15 billion would be set aside to support their possible short-term capital needs that could arise in the process of implementing economic reforms. The financial support focused on assisting crisis-affected countries to overcome their economic difficulties and to contribute to the stability of financial markets. The US and IMF supported Japan's initiative due to its bilateral nature as compared with the previous AMF proposal. Within this framework, a bilateral one-way swap agreement was also agreed between Japan and Korea (US\$5 billion) and between Japan and Malaysia (US\$2.5 billion).

### **3-2. Swap Arrangements under the Chiang Mai Initiatives**

The Chiang Mai Initiative (CMI), or regional-wide swap arrangements, was formed in 2000 on the basis of the existing ASEAN swap arrangement. The ASEAN swap arrangement dates back to 1977 when ASEAN central banks reached an agreement on its establishment by reciprocal arrangements among Indonesia, Malaysia, the Philippines, Singapore, and Thailand (the ASEAN-5). The arrangement was to provide immediate short-term swap facilities for the US dollar against the domestic currency of a requesting member country with temporary international liquidity problems. The swap transaction is for a period of one, two, or three months and is renewable once for a maximum of another three months. Each member country provides US\$20 million (total amount is US\$100 million) and a requesting country is able to borrow up to US\$40 million. In 1978, the total amount of financial resources was increased from US\$100 million to US\$200 million and each member country agreed to provide US\$40 million. Thus, a requesting country is able to borrow up to US\$80 million under the revised arrangement.

Reflecting strong voices among East Asian policy makers to strengthen financial cooperation, the leaders of ASEAN plus three (Japan, China and Korea), or ASEAN+3, held a summit in Manila in 1999 and agreed to enhance self-help and financial support mechanisms in East Asia. Subsequently, the Finance Ministers of ASEAN+3—whose total foreign reserves amounted to over US\$200 billion—agreed in May

2000 in Chiang Mai, Thailand on establishing a regional financial arrangement to supplement existing international facilities in East Asia. This “Chiang Mai Initiative” involved an expansion of the afore-mentioned ASEAN swap arrangement and was to include ten ASEAN countries (ASEAN-10) and a network of bilateral swap and repurchase agreements (BSA) among ASEAN+3. The CMI stressed a strengthening of the existing swap arrangement initiated by ASEAN and its nature as supplementary to the IMF facilities. The expected financial support from the plus three countries to ASEAN was based on a bilateral agreement, as compared with the multilateral arrangement previously sought for the AMF. Further discussion was undertaken at the 7<sup>th</sup> meeting of the ASEAN Central Bank Forum in August 2000 with an aim to expand the membership of the ASEAN swap arrangement by including the remaining members and also by enlarging the size of the facility. In November 2000, the total amount available for swap arrangements under the ASEAN swap arrangement was increased from US\$200 million to US\$1 billion.

Regarding the BSA between ASEAN and the plus three countries, and among the plus three countries, the arrangement was to supplement existing international financing facilities including those of the IMF. It had been agreed that member countries would be able to withdraw funds without any linkages to IMF programs through this arrangement, provided that the amount borrowed would be within 10 percent of the maximum amount determined. Each member country would enter into a bilateral agreement with each other at their discretion with respect to the terms and conditions of the swap transactions undertaken.

At the ASEAN+3 Finance Ministers’ Meeting in May 2005, finance ministers agreed to take the following measures to enhance the effectiveness of the CMI (called the “Second State”): (1) integration and enhancement of ASEAN+3 economic surveillance into the CMI framework, (2) defining of the swap activation process and the adoption of a collective decision-making mechanism, (3) a significant increase in the size of swaps, and (4) improvement of the drawdown mechanism. The total amount available for the ASEAN swap arrangement was expanded further from US\$1 billion to US\$2 billion.

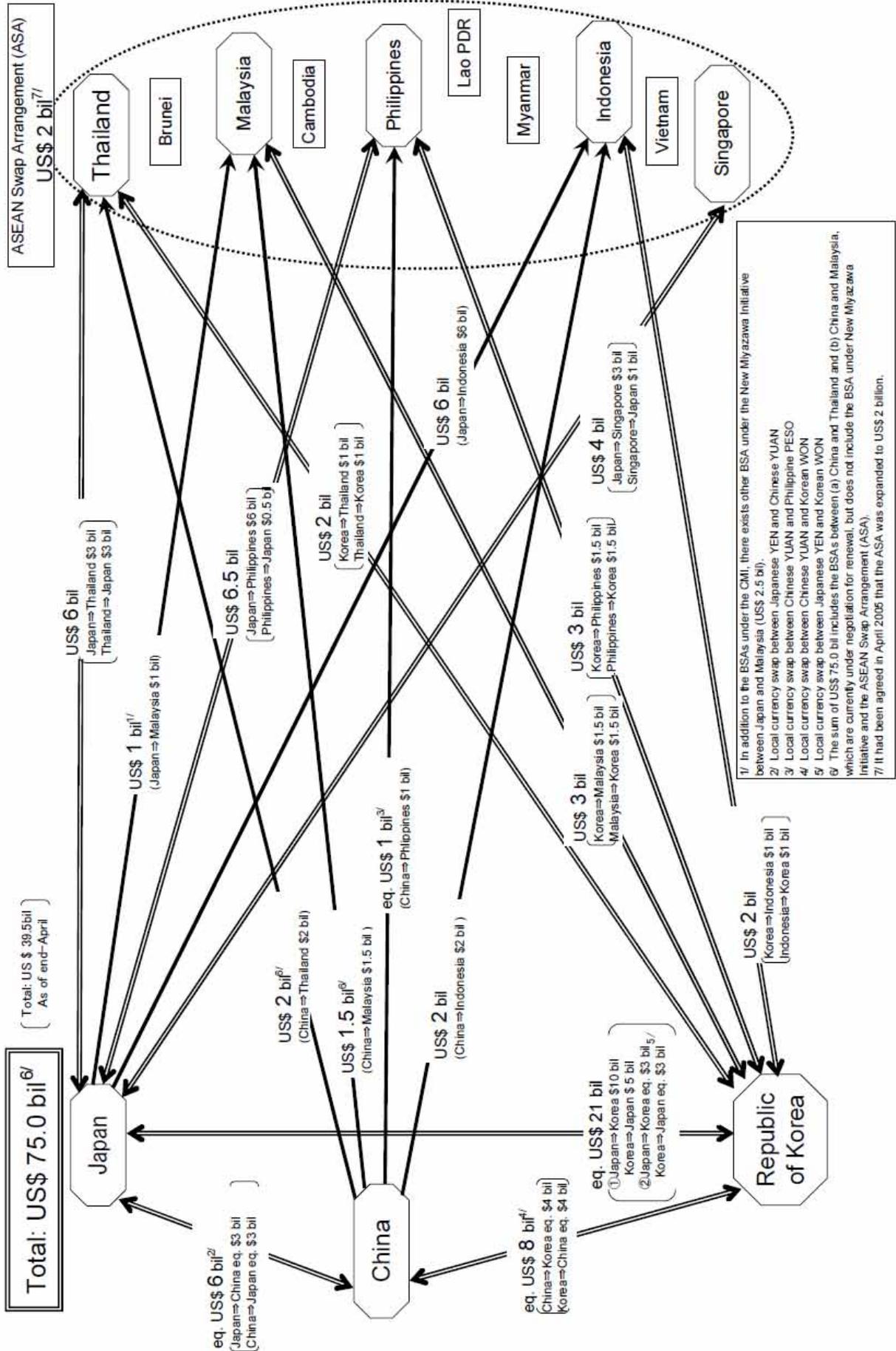
Following this agreement, in August 2005 Japan and Indonesia replaced the existing BSA (a one-way BSA between the US dollar and rupiah for up to US\$ 3 billion agreed in February 2003) with a new one-way BSA between the US dollar and rupiah for up to US\$ 6 billion. Japan and Singapore also replaced their existing BSA (a one-way BSA between the US and the Singapore dollar of up to US\$ 1 billion agreed in November 2003) with a new two-way BSA (a) between the US and the Singapore dollar for up to US\$ 3 billion from Japan to Singapore and (b) between the US dollar and the yen for up to US\$ 1 billion from Singapore to Japan in November 2005. Similarly, in February 2006 Japan and Korea replaced their existing BSA (a one-way BSA between the US dollar and the won for up to US\$5 billion under the New Miyazawa Initiative and for up to US\$ 2 billion agreed in July 2001 under the CMI) with a new two-way BSA (a) between the US dollar and the Korean won for up to US\$ 10 billion from Japan to Korea and (b) between the US dollar and the yen for up to US\$ 5 billion from Korea to Japan. In addition, in May 2005 Japan and Korea concluded a two-way BSA between the yen and won for up to an amount equivalent to US\$ 3 billion. Recently, in May 2006 Japan and the Philippines replaced their existing BSA (a one-way BSA between the US dollar and the peso for up to US\$ 3 billion agreed in August 2001) with a new one-way BSA between the US dollar and the rupiah for up to US\$ 6 billion.

Under the Second Phase of CMI, the size of the swap that could be withdrawn without IMF-supported programs has been increased from 10 percent to 20 percent of the total swap amount. In the BSA, the condition of the swap activation has been linked to the Swap Requesting Party's participation in the ASEAN+3 Economic Review and Policy Dialogue. As of February 2006, the total amount involved in BSAs under the initiative amounts to US\$71.5 billion, covering 16 arrangements among China, Indonesia, Japan,

Korea, Malaysia, the Philippines, Singapore and Thailand (Chart 1). So far, no countries have utilized the BSA thanks to the ample amount of foreign reserves accumulated in each country and the absence of any crisis. The development of this regional financial cooperation is a welcome step, as it provides liquidity for countries that might suddenly suffer a balance of payments problem under a capital account crisis and thus it should help to prevent a crisis from further deepening.

Nonetheless, there is still a need to greatly expand the scope of the BSA network under the CMI in order to promote financial stability and sustainable growth in the region. In particular, the agreement—that any financing over 20 percent of the amount available under the BSAs should be conditional on an IMF program—needs to be further amended to develop a more autonomous arrangement. The arrangement needs to be designed in such a way that funds can be disbursed quickly to manage a crisis, but that at the same time the problems of moral hazard are minimized by effective monitoring, and measures are taken to prevent a further crisis. Also, the CMI does not have its own permanent organization with a surveillance mechanism to monitor the macroeconomic, financial and capital flow trends of participating countries. Discussion about the establishment of an institution with a mandate for regional surveillance needs to be launched in the near future. Ultimately, this type of regional cooperative network should permit more flexible and timely financing measures and be able to make greater amounts of assistance available, by evolving bilateral arrangements into multilateral ones, while taking measures to avoid unnecessary duplication of IMF activities and also addressing possible moral hazard problems.

Chart 1. Network of Bilateral Swap Arrangement under the Chiang Mai Initiative



## **4. Regional Bond Market Initiatives**

### **4-1. Asian Bond Market Initiatives**

One way to deal with the afore-mentioned double mismatches and, at the same time, to mitigate unnecessary external finance is to develop domestic-currency-denominated (or domestic) bond markets. Reflecting this commonly shared view, policy makers, international financial organizations, academics, and the media have paid attention to the idea of developing domestic bond markets in East Asia after the earlier crisis. This is because domestic bond markets could provide stable sources of longer-term domestic currency funding to domestic firms, and in the process help to reduce double mismatches and strengthen financial sector resilience. In addition, domestic bond markets might help to improve the efficiency of resource allocation through market-determined interest rates, spreading various borrowers' credit risks among a large number of dispersed investors, and serving as a buffer when banking sector problems occur. Moreover, domestic bond markets also help to enhance the transparency of financial institutions' through information disclosure.

Nevertheless, the reality is that domestic bond markets were largely underdeveloped in East Asia. This was mainly because (1) there were only a small number of large, reputable private firms that could regularly issue a large amount of corporate bonds at relatively low costs; (2) there was limited demand for long-term bonds, since (mostly risk-averse) individual investors, like households, tended to hold their assets in the form of safe and liquid bank deposits; and (3) underdeveloped informational, legal, and judiciary infrastructures prevented bond markets from developing further. Given these constraints, it was not cost-ineffective to develop domestic bond markets in each country.

Since the crisis, many countries have made efforts to develop domestic corporate bond markets. However, fixed costs for establishing institutional infrastructures are relatively high and economies of scale are limited in small individual markets. As cost-effective and sound bond markets don't exist, many firms have been discouraged from raising funds from a bond market and so continue to depend on cheaper bank loans. Instead of developing individual domestic bond markets, many countries have begun to focus on the idea of developing a regional bond market in East Asia. This could exploit economies of scale by regionally incorporating a larger number of issuing firms and investors—thereby, raising both supply and demand for bonds. Moreover, this regional bond market could help diversify corporate financing, provide extra investment avenue, and better tap and more effectively mobilize not only abundant regional financial resources but also improve corporate reputations within East Asia.

Given this background, the Asian Bond Markets Initiative (ABMI) was proposed by Japan in December 2002 at an Informal Meeting of ASEAN +3 Financial Ministers Meeting. This was subsequently endorsed at the ASEAN+3 Finance Ministers Meeting in Manila in August 2003. Activities of the ABMI focus on (1) developing robust primary and secondary bond markets by expanding a wide variety of issuers and products (expanding the supply base), and (2) enhancing market infrastructure. As for the first purpose of developing markets, the following six issues have been recognized as important steps: sovereign bond issuance by governments to establish benchmarks; issuance by government financial institutions; creation of asset-backed securities markets, including collateralized debt obligations (CDO); bond issuance in the region by international development banks and government agencies; bond issuance in the region for funding foreign direct investment in the region; and expansion of local currency-denominated bonds and introduction of currency-basket bonds.

In respect to the second purpose, to enhance market infrastructure, it is crucial that an environment conducive to active participation by both issuers and investors exists, in order to develop efficient and

substantial domestic and regional bond markets. In this context, the following six issues are regarded as important: provision of credit guarantees through the active use of existing guarantors, and the possible establishment of an Asian Regional Guarantee Facility; a strengthened rating system through domestic rating agencies, and the possible establishment of an Asian Credit Rating Board; a mechanism for disseminating information on issuers and credit rating agencies; foreign exchange transactions and settlement issues on cross-border transactions; capacity building by conducting market research and technical assistance programs to promote policy dialogue and human resources development among member countries; and legal and institutional infrastructures, such as corporate laws, securities transaction laws and tax laws.

Consequently, in August 2003 at the ASEAN+3 Finance Ministers' Meeting six voluntary working groups were established at intergovernmental levels to address the afore-mentioned key areas for bond market development. The groups encompass the following:

WG1: new securitized debt instruments,  
WG2: credit guarantee and investment mechanisms,  
WG3: foreign exchange transactions and settlement issues,  
WG4: issuance of bonds denominated in local currencies by international development banks, foreign government agencies, and Asian multinational corporations,  
WG5: rating systems and information dissemination on Asian bond markets, and  
WG6: technical assistance coordination.

At the informal ASEAN+3 Finance and Central Bank Deputies meeting in November 2003, ASEAN+3 agreed to establish a Focal Group (FG) to coordinate the work of the six working groups. This would further strengthen the ongoing work of the ABMI. The FG met for the first time in March 2004 in Manila, and now monitors the progress of the working groups and coordinates their future action plans.

Since the establishment of the six working groups, ASEAN+3 officials have conducted regular dialogues and discussions among themselves as well as holding talks with academics, think tanks and the private sector, to exchange views. As some proposals have already been implemented as reported in Section 4-3 below, some of the working groups have completed their designated tasks. Against these developments, the ASEAN+3 Finance Minister's Meeting in May 2005 endorsed the reorganization of the ABMI working groups and the following changes occurred:

(a) establishment of an Ad-hoc Support Team for the Focal Group (ASTFG) and the transfer of the role of promoting information dissemination from the WG5 to ASTFG;  
(b) conclusion of the operations of WG4 on local currency bond issuance by international development banks, etc., upon completion of the group mission;  
(c) renaming WG5 on rating systems and information dissemination as WG4 on rating systems;  
(d) conversion of WG6 to the TA Coordination Team for the Focal Group

At the same meeting, the Finance Ministers also agreed to take the following measures to further contribute to the development of deeper and more liquid regional bond markets: (1) introduction of an ABMI roadmap that proposes (i) a new framework to gather and share information on bond market development in an integrated manner, (ii) regular self-assessment by member countries on impediments to investment that have been pointed out by market participants, and (iii) the launch of a study on Asian currency basket bonds;

(2) commencement of a study of “Asian Bond Standards” to explore the development of international bond markets in Asia; and (3) embracing the voluntary “practical alternatives” for withholding tax treatment on bond holding.

#### **4-2. The Asian Bond Fund As a Way to Expand the Demand Base**

Since mid-2002, Thailand and its then Prime Minister, Thaksin Shinawatra, has been a strong proponent of an Asian regional bond market. In particular, Thailand proposed the establishment of an Asian Bond Fund (ABF), where regional governments voluntarily contribute 1 percent of their foreign reserves (which would amount to US\$1.3 trillion) to a fund designed to purchase regional bonds. Thailand’s ABF proposal to jointly develop an Asian regional bond market using the region’s ample foreign reserves finally culminated in an agreement at the Second Ministerial Meeting of the Asia Cooperation Dialogue Forum in Thailand in June 2003.

The ABF was launched, with an initial balance of about US\$1billion (US\$100 million from the Bank of Japan), under the Executives’ Meeting of East Asia and Pacific Central Banks (EMEAP) Group, comprised of the central banks of 11 countries in the region (Thailand, Indonesia, Malaysia, Singapore, the Philippines, China, Hong Kong, Korea, Japan, Australia, and New Zealand). EMEAP was established in 1991 as a cooperative organization of monetary authorities and central banks in East Asia. Since 1996, the structure of the EMEAP has been strengthened against the background of the increasing interdependence of member economies. The first EMEAP Governors’ Meeting, hosted by the Bank of Japan in July 1996, decided to hold Governors’ Meetings once a year and to establish two working groups (financial Market development and central banking operations) and one study group (banking supervision) to undertake studies on the primary functions of central banks. The EMEAP launched the EMEAP Internet in July 1998 by connecting all member central banks with an electronic network that allowed for the quick exchange of information among members. The ABF is managed by the Bank of International Settlements (BIS) and invested in a basket of US dollar-denominated bonds issued by Asian sovereign and quasi-sovereign issuers in eight EMEAP economies (China, Hong Kong, Indonesia, Korea, Malaysia, Philippines, Singapore, and Thailand).

In April 2004, EMEAP announced plans to launch a second bond fund (ABF-2). In December 2004, the establishment of ABF-2 was officially announced by EMEAP with a new fund of US\$2 billion. The Bank of Japan decided to subscribe to ABF-2 that was to invest in local Asian currency-denominated bonds. The amount of the BOJ subscription was up to US\$ 200 million. ABF-2 aims to promote the development of bond markets in East Asia, building on the successful launch of the first stage of the Asian Bond Fund (ABF-1) in June 2003. While ABF-1 invests in US dollar-denominated bonds issued by sovereign and quasi-sovereign borrowers, ABF-2 is supposed to invest in domestic currency-denominated bonds issued by sovereign and quasi-sovereign borrowers in the eight EMEAP markets.

ABF-2 comprises two separate vehicles for investment in local-currency denominated bonds: the Fund of Bond Funds and a Pan-Asian bond Index Fund. The Fund of Bond Funds invests in bond funds in individual markets, which would in turn be invested directly in bonds. The Pan-Asian Bond Index Fund invests directly in the region’s local currency denominated bonds, aiming at offering international investors a means of exposure to a broad range of local-currency denominated bonds across the region. Moreover, ABF-2 is open to investment by private- as well as other public-sector investors. The launch of ABF-2 is a welcome step as it might promote the development of local currency-denominated bond markets in the region. ABF-2 began operating in June 2005.

### **4-3. Recent Initiatives to Develop the Supply Base**

In line with the ABMI, since 2004 the Asian Development Bank (ADB) has begun to actively issue local-currency denominated bonds in order to expand the supply base. The currencies issued so far cover the rupiah, Hong Kong dollar, Singapore dollar, Malaysia ringgit, Thai baht, and the Chinese yuan. The World Bank and the International Finance Corporation have also issued local currency-denominated bonds. The ADB has also launched an Asian Bonds Online Website to disseminate information on the region's bond markets.

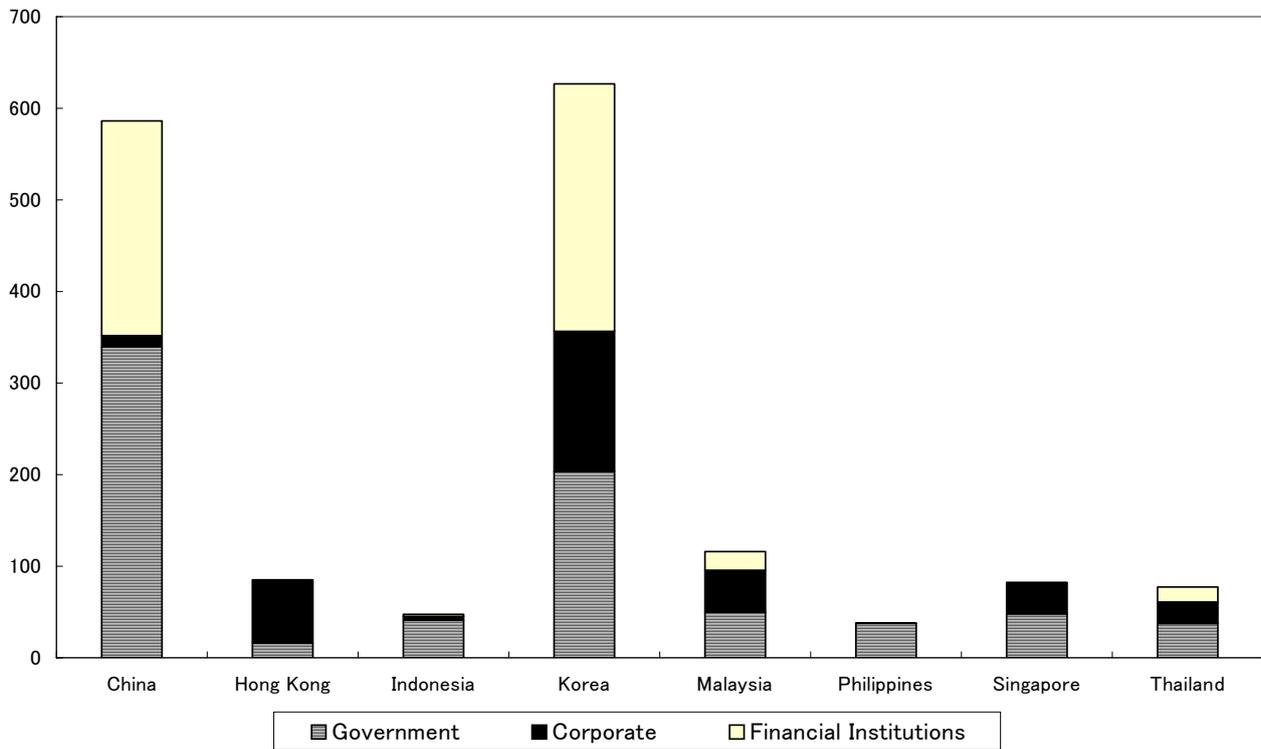
Japan has been active in promoting ABMI by initiating several measures to expand the supply base. From April 2004, baht-denominated bonds have been issued by Japanese subsidiaries in Thailand with a partial credit guarantee from the Japan Bank for International Cooperation (JBIC) and Nippon Export and Investment Insurance (NEXI). Also, since June 2004 the JBIC has provided guarantees to local-currency denominated bonds issued by Japanese firms operating in Thailand.

In June 2004, Japan and Korea agreed to work together to promote the development of asset-backed securities markets in Asia, in line with the Asian Bond Markets Initiative. They pledged their joint effort in proposed cross-border yen-denominated Korean collateralized bond obligations (CBO), the so-called "Pan-Asian bond," that would provide financing to SMEs in Korea. The underlying portfolio would comprise of a pool of SME loans or bonds that would be selected by a credit committee jointly managed by the Industrial Bank of Korea and the Small Business Corporation of Korea. The issuance would be in the form of senior and subordinated bonds, with the Small Business Corporation of Korea subscribing to the subordinated bonds thereby providing the first loss protection to capital market issuance. To appeal to a broad spectrum of investors in Asia, however, the Korean government is prepared to have the Industrial Bank of Korea to extend a fully covered credit facility to support the timely payment of senior obligations under the senior bonds (as a first layer guarantee). Japan would help this process by enhancing the guarantee operations of the JBIC as a second layer guarantee. In doing so, Japan amended the Ministerial Notification governing the JBIC guarantee policy, thereby legitimizing the function of the JBIC to take a more proactive role in its guarantee operations for appropriately structured and credit enhanced debt instruments within the region. The CBO would be internationally issued for placement by incorporating these dual guarantee structures, so that they could tap into the Asian investor base and provide much needed liquidity to the Korean SME sector at an extremely competitive rate. The JBIC had already begun its deliberations to issue guarantees with the inaugural launch of the CBO.

In August 2005, the JBIC issued Japanese government-guaranteed, fixed interest Thai baht bonds in Thailand. These baht bonds were the first regional currency bond issuance undertaken by the Japanese issuer in line with the ABMI. In May 2004, Thailand indicated its guidelines for approving, on an individual basis, bond issuance by foreign governments and official financial institutions. In response, the JBIC launched a series of discussions with Thailand and obtained approval for baht bond issuances. The baht funds obtained from these issuances would be used for financing business operations of Japanese firms in Thailand through Bangkok branches of Japanese banks (i.e., Tokyo-Mitsubishi Bank, Mizuho Corporate Bank and SMBC). These issuances have made it possible to provide local currency financing without currency exchange risks. In this way it is expected to meet the comprehensive financial needs of local Japanese affiliates. In September 2005, the JBIC signed a two-step loan agreement totaling up to 3 billion baht, with each of Tokyo-Mitsubishi Bank, Mizuho Corporate Bank and SMBC providing one billion baht. The funding of this loan comes from the baht bonds the JBIC issued. Reflecting the growing numbers of sovereign bonds issued, the size of outstanding local currency-denominated bonds has expanded in many

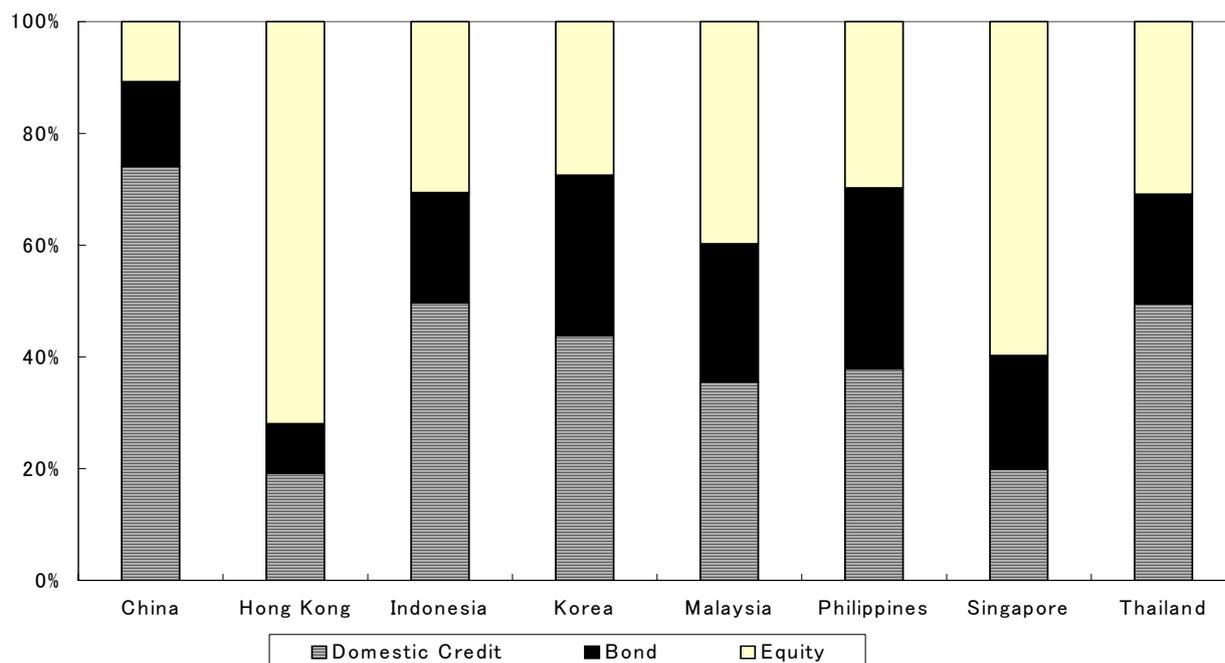
East Asian countries since the crisis. Malaysia and Korea have attempted to extend government yield curves by issuing longer maturity bonds. Efforts are also being made by Indonesia, Korea, Malaysia, the Philippines, and Singapore to increase the issue size of benchmark government bonds. The increase in the size of the bond market can largely be explained by the expansion of government bonds in China, Indonesia, Korea, and the Philippines; reflecting a deterioration of the fiscal balance and a need to raise funds to finance financial and corporate restructuring. By contrast, the bond market expanded sharply mainly as a result of the development of corporate bonds in Hong Kong and Malaysia. The corporate bond market in Korea has also moderately increased. In the case of Singapore, both government and corporate bonds have rapidly expanded. In terms of relative size, the amount of outstanding total bonds issued has been larger in China and Korea than in other countries (Chart 2). Chart 3 indicates the relative size of outstanding local currency-denominated bonds, equity and domestic credit. Reflecting the bond market development, many Asian countries now have more balanced financial and capital market structures, as compared to those prior to the crisis.

**Chart 2. Sizes of Outstanding Local Currency-Denominated Bonds  
(US\$ Billions, as of September 2005)**



Source: Asian Development Bank, Asian Bonds Online.

**Chart 3. Domestic Financing Profile (As a Percent of Total, as of September 2005)**



**Source: Asian Development Bank, Asian Bonds Online.**

Nevertheless, the market for local currency-denominated corporate bonds needs to be expanded and deepened in East Asia. While the ABMI is already being promoted under the ASEAN+3 Finance Ministers' Process, the issues involved in establishing sound infrastructure (i.e. accounting and auditing standards, settlement systems, credit rating agencies, guarantee systems) need immediate discussions and to be promoted. This would lead to increasing the amount of supply and demand for bonds. To expand the demand base, it is important to consider an increase in the amount of ABF-2 issues, as this will facilitate an increase in public sector investments in regional currency denominated bonds.

Furthermore, Japanese corporations operating overseas have so far been mostly procuring funds from their parent companies in Japan. In the future, these corporations are likely to increasingly need to procure local currency-denominated funds by issuing bonds and borrowing from domestic financial institutions. To encourage the growth of bond-issuing markets for these firms, government-sponsored financial institutions, such as the JBIC or NEXI, should increase the amount of their guarantees to encourage the issue of local currency- denominated bonds in East Asia until the bond-issuing organizations are highly recognized and gain creditworthiness. In addition, consideration should be given to obtaining the cooperation of the ADB to establish regional credit guarantee organizations. Such organizations would also help guarantee confidence in Japanese and other corporations operating in Asian countries that have local currency denominated bonds.

Furthermore, the asset-backed securities (ABS) market should be further developed based on Japanese corporate financial credits held by non-Japanese Asian corporations in East Asia, and vice-versa. This type of diversification of financing instruments would effectively stimulate demand for local bonds. Another front would be the privatization of the Japan Post Office, expected to occur from 2007, and to develop a more efficient asset management system in the medium to long run. This is likely to create a strong institutional investor in the region, and will encourage investments in financial and capital markets not only in Japan but also in East Asia.

To improve market infrastructure, it is also important to establish favorable regional arrangements, such as agreements on withholding taxes on profits, dividends, and interest. As redemptions of securities procured, transmissions of profits and dividends, and transactions between subsidiaries and their parent companies increase in the region, such arrangements will become important to support intra-regional private sector activities. Regional coordination with a view to eliminating cross-border investment barriers with the standardization and harmonizing of relevant legislation and taxation systems is another important item on the regional agenda that should be given immediately attention.

## **5. Movements towards Regional Currency Cooperation**

### **5-1. Exchange Rate Policies and a Trilemma**

It is well known that a large number of emerging market economies face a trilemma: the impossibility of simultaneously achieving (1) exchange rate stability, (2) full capital account liberalization, and (3) monetary policy independence (or domestic interest rate management). First, if a country attempts to achieve exchange rate stability and monetary policy independence, it needs to introduce capital controls. Controls over capital flows would allow countries to select domestic interest rates independently of those set in other countries and maintain stable exchange rates despite interest rate differentials. Second, if a country attempts to achieve exchange rate stability and full capital account integration, a very rigid fixed exchange rate regime, such as the currency board system or a currency union, should be considered by abandoning monetary policy independence. Third, if a country chooses independent monetary policy and full capital account liberalization, strict fixed exchange rate regimes would not be an option in the presence of massive capital movements driven by interest rate differentials and possibly frequent speculative currency attacks.

With recent global trends toward capital account liberalization, countries have been increasingly facing a choice of exchange rate stability (fixed exchange rate regimes) or monetary independence (flexible exchange rate regimes with inflation targeting). In particular, since the East Asian crisis, the choice over exchange rate regimes has become an important agenda for emerging market economies, since an appropriate choice of regimes could function as a crisis prevention measure.

In the phase immediately after the crisis, the world paid attention to so-called “two-corner solutions” of exchange rate regime choices, as being choices preferable to “intermediate” regimes. That is, a flexible exchange rate regime (i.e., free float or managed float with limited intervention) as one corner and a strict fixed exchange rate regime (i.e., currency board, full dollarization or currency union) as the other corner. The preference toward a strict fixed exchange rate regime arose from the observation that countries with open capital accounts were not able to maintain stable exchange rates, unless adopting a very rigid (or credible) fixed exchange rate regime so that any currency speculations driven by the expectation of a regime change would be trimmed. A credible fixed exchange regime could also function as the nominal anchor for monetary policy, since the lack of discretionary monetary policy eliminates inflationary bias, thereby lowering interest rates and expanding economic growth. On the other hand, a free float regime is also preferable, since limited government intervention and resultant volatile exchange rate movements would discourage speculative capital flows due to greater exchange rate risks, while allowing for an independent monetary policy. Supporters of two-corner solutions postulate that the East Asian crisis happened because these countries had adopted soft-pegs with loose commitments, which can be categorized as intermediate exchange rate regimes.

However, since the collapse of the currency board in Argentina in 2001, middle-ground exchange rate regimes have re-gained their popularity. This support also reflects a “fear of floating,” a tendency for a

country to become reluctant to freely float its exchange rates even though it claims to have adopted a free float, for fear of excessive volatility and a reduced ability to control inflationary expectations, as pointed out by Calvo and Reinhart (2002). A country with a substantial amount of foreign debt, an extensive trade orientation, and a high degree of pass-through, has an incentive to reduce exchange rate volatility. Particularly, a country with a substantial amount of dollar-denominated external debt and invoicing of trade transactions tends to stabilize its currency against the dollar. As a result, the exchange rate regime of such a country appears similar to a fixed exchange rate regime.

Middle-ground exchange rate regimes traditionally include a “crawling peg” that has its parity adjusted periodically based on past inflation differences with a major economic partner and a “target zone” that allows the exchange rate to fluctuate within a band. Meanwhile, a regime that has gained popularity among academics in recent years is a “crawling basket peg with a band”—the so-called a “BBC” (band, basket, and crawl) approach proposed by Williamson (1999, 2000). The basket pegs consists of international currencies, such as the dollar, euro, and Japanese yen, and should provide some cushion against third-party exchange rate movements for countries with a diversified pattern of trade and financial relationships with major industrial countries. The weights can be determined based on trade volume, thereby placing greater weights on the yen and euro relative to the dollar peg adopted prior to the crisis. The crawl is supposed to reduce the chance of facing real exchange rate misalignments, which can often be caused by growing inflation differentials and thus deteriorating international price competitiveness against trade partner countries. The crawl or an adjustment of the central parities of nominal effective exchange rates could be either backward-looking (to offset recent inflation differentials) or forward-looking (to offset projected future inflation differentials). The band needs to be wide enough (i.e., plus and minus 15 percent) to allow for some flexibility to deal with various exogenous asymmetric shocks and to give a certain degree of independent monetary policy.

## **5-2. De Jure and De Facto Exchange Rate Regimes**

In examining the exchange rate regimes actually adopted by East Asian countries, both “de jure” (officially announced) and “de facto” regimes have to be considered, as they often differ. For example, there is the case where a country heavily intervenes in the foreign exchange market and thus adopts a de facto fixed exchange rate regime, notwithstanding that the publicly announced exchange rate regime is a free float. Information on de jure exchange rate regimes can be obtained from the IMF Annual Report on Exchange Rate Arrangements and Exchange Restrictions (as reported for selected East Asian countries on the first row of Table 2). The IMF report for 1996-97 adopted four classifications (peg, limited flexibility with a basket, managed float, free float; listed by their order of rigidity), and in 1998 reclassified them into eight more detailed classifications (no separate legal tender, currency board, peg, peg within horizontal bands, crawling peg, crawling band, managed float, independent float). A regime of no separate legal tender indicates a currency union.

The table indicates that the de facto exchange rate regime for Thailand was a regime of “limited flexibility with a basket,” while the regimes for Indonesia, Korea, and the Philippines were classified as a (more flexible) “managed float”. After the crisis, all four countries shifted to a (most flexible) “independent float”, leaping to one corner of the regime choices. Before 1998, the Chinese regime was classified as a managed float, but since 2002 it has been classified as a peg owing to the narrowing of the band (until the adoption of a new exchange rate regime in July 2005). Similarly, Malaysia shifted from a managed float to a peg in September 1998 (but has since July 2005 adopted a basket peg following China’s exchange rate

reform). Singapore has maintained a managed float from before the crisis and continues to do so after it.

On the other hand, a de facto classification adopted by Reinhart and Rogoff (2004) is to classify regimes based on information about the actual monthly movements of official and dual (parallel) rates along with historical information about exchange rate regimes. According to this de facto classification (as reported in the second row of Table 2), Indonesia and Korea have shifted from a crawling peg to a free float (or an independent float); Thailand and the Philippines from a peg to a managed float. Compared with the de jure classification, the de facto regimes for these countries indicate greater rigidity before the crisis, while both classifications show an increase in flexibility after the crisis. Thus, the de facto classifications appear to be more consistent with the generally shared view that crisis-affected countries had adopted a dollar peg or a rigid exchange rate regime prior to the crisis.

**Table 2. Classifications of Exchange Rate Regimes in East Asia**

IMF De Jure Classification		
	1996	2002
Indonesia	Managed float	Independent float
Korea	Managed float	Independent float
Thailand	Limited flexibility with a basket	Independent float
China	Managed floating	Peg
Philippines	Managed floating	Independent float
Malaysia	Managed floating	Peg
Singapore	Managed floating	Managed float
De Facto Regime		
	1996	2001
Indonesia	De facto crawling peg	Freely float
Korea	De facto crawling peg	Freely float
Thailand	De facto peg	Managed float
China	De facto peg	De facto peg
Philippines	De facto peg	Managed float
Malaysia	Limited flexibility	Peg
Singapore	De facto moving band	Managed float

**Source: Shin K. and J. Lee (2004).**

### **5-3. Cooperation towards Common Currency Arrangements**

In the long run, some coordination of currency arrangements aimed at a common currency union could be a viable option in East Asia. Currency arrangements to stabilize regional exchange rates are likely to promote trade and investment linkages, thereby bringing about coordinated business cycle movements and a convergence in per capita income levels. The fact that intra-regional trade already exceeds more than 50 percent in the East Asian region supports such a move toward mutual currency arrangements. The vision for currency cooperation aims to stabilize exchange rate volatility vis-à-vis major international currencies (i.e. US dollar, yen and euro) and intra-regional exchange rate volatility.

Currently, East Asian countries have diverse exchange rate regimes; indeed some economies have expressed strong commitments to maintaining the existing exchange rate regimes. For example, since 1983 Hong Kong has adopted a currency board system. China carried out exchange rate reform in July 2005 with a 2.1 percent revaluation of the yuan against the US dollar and the adoption of a BBC-type regime; however, until today the yuan has continued to remain quite stable against the US dollar as a result of heavy

intervention in the foreign exchange market by Chinese authorities. Since 1973 Singapore has adopted an exchange rate arrangement similar to the BBC system, with a trade-weighted currency basket comprising the US dollar, yen, euro and other regional currencies, and has regularly modified the band by taking into account the changes in economic fundamentals. By contrast, since the crisis, Korea, Thailand, and Indonesia have adopted either free or managed floats, together with inflation targeting.

Thus, it obviously will take some time for the East Asian countries with their diverse economic structures to set in place structures encouraging currency coordination within the region. While the region's member countries remain so diverse in economic structures and development stages, they are likely to face asymmetric macroeconomic shocks. In such cases, countries are inclined to adjust their exchange rates to absorb shocks, thereby reducing any incentive for currency coordination. At this stage, the political will for such policy coordination is not strong. While the idea of a common currency union has occasionally been discussed in the context of ASEAN, any immediate application appears unlikely because ASEAN member countries differ substantially in terms of their degrees of capital account convertibility and economic structures, and many local currencies are not international ones. Such differences make it extremely difficult, particularly for some economically weak ASEAN member countries, to discuss the loss of monetary policy independence and the limited use of fiscal policy envisioned under European Monetary Union. At the same time, however, the difficulty excluding Asian countries with weaker currencies from such a discussion table would make it an even more difficult task to realize cooperation.

As regional economies become more integrated and income levels converge through market forces, as a first step each country could begin by adopting a BBC-type regime with weights determined individually by bilateral trade volumes. By adopting a basket peg against the weighted value of the US dollar, yen, euro, and some other major regional currencies, the region could reduce exchange rate volatility. This basket currency composition is reasonable given the region's heavy dependence on the US, Japan, and the EU. As a second step, as the economies and trade structures of East Asian countries become further integrated and become more autonomous, East Asia may consider the adoption of a common BBC regime, with weights and basket currencies being the same among the member countries. The band could be plus and minus 15 percent or greater. A common BBC regime is superior to an individual regime since the latter generates different basket pegs so that any change in yen-dollar rates, for example, could lead to volatile exchange rates among member countries.

Alternatively, East Asia could consider the adoption of an Asian Exchange Rate Mechanism similar to the European Exchange Rate Mechanism that was introduced in 1979. Under the European Exchange Rate Mechanism, each member country adopted a central parity for its exchange rate against other member countries' currencies and was committed to keep that exchange rate within a band of plus and minus 2.25 percent (6 percent for Italy as a later entrant). An Asian Currency Unit (ACU) should comprise only Asian currencies and could also be introduced like the ECU as a weighted average of member countries' currencies and a unit of account. If the ACU served as a basket currency target, it would mean that East Asia adopted an ACU basket peg with a band and a crawl. The weights could be based on the trade volume share of each member country of the total regional trade volume. The band would need to be sufficiently large. The region would also need to introduce a short-term financing mechanism, following the "Very Short-Term Financing Facility" adopted in Europe, so that a country with a weaker currency could borrow from strong currency countries. When a particular exchange rate reaches the ceiling or floor of the band, relevant member countries should be committed to intervene in the foreign exchange market. The CMI could possibly be positioned as a Very Short-Term Financing Facility if the arrangement were to be re-designed to meet this

purpose.

The Asian Exchange Rate Mechanism could be better than a BBC-type regime, since it would follow the approach adopted by Europe and thus promote close currency and macroeconomic policy coordination. Regional exchange rate volatility is likely to be reduced substantially and the degree of income convergence could be greater, thereby further expanding trade and investment activities. Increased fluctuations of East Asian currencies against the US dollar (and euro) might encourage member countries to use East Asian currencies more frequently in their transactions. However, the major drawback is the fact any Asian Exchange Rate Mechanism would be likely to expand the volatility of exchange rates between East Asian currencies and the US dollar and euro, making it problematic for countries whose major trade partners are the US and Europe. For example, a member country which exports largely to Europe might lose its international price competitiveness by the depreciation of the euro against the yen. By contrast, the BBC-type regime is likely to better absorb yen-dollar and dollar-euro rate movements. Moreover, the adoption of a common BBC-type regime is likely to stabilize regional exchange rates to some extent, particularly through stabilizing those against movements of the US dollar, yen and euro. For this reason, the BBC-type regime is viewed by as being more appropriate for East Asia than an Asian Exchange Rate Mechanism.

In recent years, some commentators have proposed the creation of a parallel currency together with existing individual currencies (Eichengreen 2006). The parallel currency so proposed would be the ACU. East Asian countries could use it as a unit of account, a means of payment, or the store of value in domestic and cross-boarder transactions by giving it an official status. The parallel currency approach aims to encourage banks, firms, and investors to increase their ACU-denominated transactions. The region could collectively issue sovereign bonds denominated in ACU and settle cross-boarder securities transactions in ACU, thereby increasing the liquidity and efficiency of secondary markets for the ACU. As the likelihood of adopting the Asian Exchange Rate Mechanism is remote, this parallel currency approach could be more desirable as a first encouraging step toward a currency union. Parallel use of the ACU may promote the active use of the ACU. However, such a vision could be optimistic, particularly if one considers the European experience where the ECU was not actively used in settlements of trade and financial transactions, or in the denomination of international bonds and loans. Central parity (expressed in ECU) was used mostly to compute bilateral exchange rates by central banks and markets. The ECU's role as a unit of account was limited to the financial accounts of European Community (EC) institutions and a few firms (Eichengreen 2006).

Further, a combination of a BBC-type regime and a parallel currency approach could be considered as an option. While East Asian countries are encouraged to adopt a BBC-type regime, a parallel currency, such as an ACU, could be introduced in addition to each of the existing regional currencies (Williamson 2005). However, Eichengreen (2006) criticizes this option as being undesirable and mutually non-compatible because a BBC-type regime promotes the use of international currencies (such as the US dollar, yen and euro), while the Asian Exchange Rate Mechanism would encourage the use of regional currencies. In other words, under this approach the ACU would need to compete not only with existing regional currencies but also with major international currencies such as the US dollar.

In 2005, the ADB announced a proposal for introducing an ACU sometime in 2006—a step closer to a parallel approach. The ACU will be a weighted average of East Asian currencies, like the ECU, and be calculated by the ADB. The weights would be determined based on trade volumes, GDP, etc. The ACU is initially to be used as an indicator of the stability of member countries' currencies against the US dollar and

the euro, as well as vis-à-vis a currency basket (or a regional weighted average). This would allow member countries to monitor the collective movement of East Asian currencies, thereby assisting monetary authorities in their exchange rate policy formulations. The ACU is expected to include the currencies of ASEAN+3 and some other regional currencies. If East Asian countries begin to discuss and coordinate economic policies, and use the ACU as a reference, this move may eventually lead to a consensus that the fluctuations of their currencies should be contained within a certain range and so initiate moves toward currency cooperation. Since the announcement of the proposal, however, there have been disagreements among East Asian countries about which currencies should be included in its scheme. In May 2006, the Finance Ministers of ASEAN+3, meeting on the sidelines of the ADB's annual meeting, acknowledged the importance of sharing a long-term vision for financial and currency cooperation and agreed to study the usefulness of creating "Regional Currency Units". Subsequently, the ADB responded by welcoming the announcement. While detailed issues remain unanswered and it is unclear whether the regional currency units proposed are the same as the ACU announced by the ADB, this is a welcome first step toward regional currency cooperation.

The progress toward currency cooperation, regardless of whether a common BBC-type regime or the Asian Exchange Rate Mechanism, is closely associated with the internationalization of the yen. At the present time, the US dollar is by far the most dominant international currency in the region, but some argue that including the yen in a basket of currencies would help stabilize effective exchange rates, promote currency transactions between the yen and other Asian currencies, and encourage internationalization of the yen. Namely, an increase in the weight of the yen in the basket of foreign currencies may promote the use of the yen in trade and financial transactions within the region, while an increase in the actual use of yen in regional transactions may also promote a move toward a BBC type regime.

As Japan's economy has regained sustainable economic growth, and as domestic financial institutions have reduced their holdings of non-performing loans, these domestic financial institutions have also improved their financial intermediary capacity domestically and globally. Thus it is again necessary to encourage Japanese banks' overseas financing and investment activities, especially those in East Asia. It is important that Japanese banks be positioned as key players to promote the development of regional foreign exchange and financial markets that conduct direct exchange rate transactions in yen and other Asian currencies. In addition, encouraging Japanese banks to make yen- or local currency-denominated loans and to issue financial bonds in the region will increase overseas use of the yen as well as promoting bond market development—just as development of the international banking market in Europe contributed to the internationalization of the euro. Since Japanese firms are increasing foreign direct investments in East Asia, the role of Japanese banks is in parallel becoming important. If Japanese banks could establish financial networks in the region, overseas Japanese corporations, their affiliates and partner companies would be able to develop efficient cash management mechanisms involving a networking system to pay only net gains from their mutually held credits and liabilities. This would facilitate business activities and reduce operating and financial costs for all involved. It would also increase the need to strengthen financial sector governance in Japan and the region, improve prudential regulations, and increase the effectiveness of financial institution management systems.

Finally, a major precondition to promoting financial cooperation in East Asia is the internationalization of Japan's financial and capital markets. To promote internationalization, measures should first be taken to encourage non-resident investors to invest in those markets. But such potential investors would not do so unless Japan's financial and capital markets are made more attractive, and this will

not occur until more information is disclosed. Recently, Japan has introduced measures for the sale of its sovereign bonds in Europe, the US and East Asia (to prepare for major refinancing projects anticipated as coming in the near future). This measure should likewise be pursued more actively in East Asia and so increase demand from regional institutional investors for yen-denominated assets. To further promote yen-denominated capital procurements by non-residents, and to offer better terms for capital procurements through Samurai Bonds (yen-denominated bonds issued in Japan by a non-Japanese issuer), consideration should be given to making issuing conditions more cost-effective and reducing the clerical load. It would also be advisable to introduce measures stimulating the Samurai Bond market, and to promote investments by Japanese investors in Samurai Bonds. Furthermore, promotion of Japan's FTA and EPA would increase the proportion of yen-denominated account settlements and would thus encourage greater use of the yen.

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## 4. Political and Security Cooperation in East Asia?

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### Introduction

Friedberg contends that East Asia is “ripe for rivalry and a place likely to emerge as the “cockpit of great-power conflict.”<sup>1</sup> Does this assertion truly apply? If it does apply, it certainly applies to the political and security areas. In East Asia, the development of regionalism has been led by economics, in particular trade, as discussed in Chapters Two and Three. Regionalization of economies in East Asia has led regionalism. Regionalism involves the process of institution creation to promote regional cooperation. Such institutions are designed to deal with transnational issues faced by countries in the region. In contrast regionalization is a natural process for regional cooperation as has been the case of East Asian economies. According to 2003 statistics, the ratio of intra-regional trade in East Asia, while lower than that of the European Union (EU), was higher than North American Free Trade Agreement (NAFTA’s) in terms of exports. Deepening trade interdependence has motivated countries in East Asia to either conclude or negotiate Free Trade Agreements (FTAs) or more comprehensive versions of Economic Partnership Agreements (EPAs). Region-wide FTAs or EPAs has also been on the table for discussion. Witnessing interconnected financial market at the time of 1997 Asian monetary crisis, ASEAN+3 has also established initiatives for financial cooperation, including the Chiang Mai Initiative and a proposal for an Asian Bond Market, as described in Chapter Three. These initiatives were prompted by the 1997 Asian financial crisis when countries learned through the impact of a crisis in Thailand spreading to other countries in the region. This sent a message how the final market is regionalized.

However, in the political and security arenas, regional cooperation, not to mention regional integration, has been identified as a tremendous challenge at best. Sino-Japanese rivalry and surging nationalism have often been cited as impediments for regional cooperation. Regionalization in the political and security areas has surely been limited but has recently been on the rise on non-traditional transnational security issues. Meanwhile regionalism in East Asia has not been promoted consciously enough to lead regionalization of security. The post Cold War or post-post Cold War East Asia is still divided, with national security and sovereignty still strong in the perceptions. East Asia has therefore elements of competitive security that demands traditional deterrence and crisis response mechanisms against the backdrop of the remaining flashpoints from the Cold War namely Korean peninsula and Taiwan straits. Moreover, Sino-US military confrontation cannot be excluded with the recent build up of Chinese military power which is reportedly beyond the need for the contingency over Taiwan straits. US Department of Defense in its annual report to congress on *Military Power of the People’s Republic of China* in its 2006 edition stated that “China has the greatest potential to compete militarily with the United States and field disruptive military technologies that could over time offset traditional U.S. military advantages.”<sup>2</sup> Moreover with the advent of globalization and trigger by 9.11, non-traditional security threats are gaining higher profile than ever before in East Asia which increases the need for cooperative security and common security approach in the region. In analyzing East Asia, we need to employ all three theories of international relations, namely realism that considers balance of power and national confrontations, but also liberalism that tries to promote security by multilateral institutions as well as constructivism that promotes security system based not on power but on

norms.

In hindsight, the building of a comprehensive East Asian community could not have been a topic of discussion during the Cold War. The region has long been fragmented and has not shown any signs for cohesion. However, with the end of the Cold War, in part due to the impact of the movement towards further regional integration in Europe, nations in the Asia Pacific region established the Asia Pacific Economic Cooperation (APEC) conference in November 1989, incidentally in the same month that the Berlin Wall, the symbol of the Cold War, was dismantled. Given the success of APEC, in the post Cold War setting the process was expanded beyond economy, and the ASEAN Regional Forum (ARF), an intergovernmental multilateral security dialogue process, was launched in 1994. It is worth noting that the regional process established in the 1990s took the format of *ASEAN+X* rather than a pure multilateral form. The most notable example of this framework was *ASEAN+3*, the three being Japan, China and South Korea, created in 1997. The *ASEAN+3*'s 1999 Joint Statement on East Asia Cooperation took the unprecedented and significant step of including transnational political and security issues as areas of cooperation, in addition to cooperation in the traditional economic field.<sup>3</sup>

Despite this statement, however, the legacy of the Cold War still lingers in East Asia, and it can be argued that the region has a long way to go in building a collective security community. Since the end of the Second World War, many countries in East Asia have secured their national and regional security through bilateral alliances and treaties with the United States, forming the so-called hub-and-spoke architecture. It is phenomenal that these "spokes" have not developed a "wheel" amongst them. During the Cold War spokes remained tied to the hub but not each other. When it comes to a collective security community, it has been consistently argued it does not have a substantial meaning if the current East Asian security environment remains and if it does not involve its hub, the United States in post Cold War and in post-post Cold War context.

Americans have argued against an East Asia community concept, particularly after the announcement of the East Asia Summit to be held. For example Richard Armitage expressed his opposition to the concept of an East Asian community in May 2005 in an interview with the *Asahi Shimbun*, asserting that the attempt to build an East Asian community without the United States would be a serious mistake, and that China is anxious to exclude the United States from consultations.<sup>4</sup> Should community building in East Asia progress, the question of US participation in a community in one form or another must be considered. Since mid-2005, US opposition to East Asian community building and an East Asia Summit has lessened after it was decided that India, Australia and New Zealand would be added to the list of participants in the East Asia Summit, leading the United States to believe that the Summit would no longer be a China-centered process. Nonetheless, how to relate with the United States remains an issue for the discussion and practice of East Asian community building, particularly in the political and security areas.

With regard to East Asian community building, Japan has its share of opponents and proponents, in addition to those who maintain a skeptical position. Opponents of the concept deny the possibility of creating an East Asian community, even in the area of the economy, arguing that countries in the region do not share values which would form the basis of community building and thus are not ready to yield sovereignty for a regional community. Naoki Tanaka, President of the 21 Century Public Policy Institute in his report to the House of Councilors in 2005 argued that East Asia, despite its growing economic regional interdependence, cannot complete its regional economic network alone; East Asian nations rely heavily on the United States for absorption of their goods, and an East Asian Economic community excluding the United States does not make sense. Tanaka considers the Korea-US FTA negotiations currently underway as an example of a move that opposes the building of a community in East Asia.<sup>5</sup> Taro Yayama, a critic, argues

that it is impossible to consider an East Asian community that includes China, because the Chinese have been indoctrinated by the educational system to hate Japan.<sup>6</sup> Mineo Nakajima, President of Kokusai Kyoyo University also argues that East Asia's political and cultural diversity is too overwhelming to make economic or functional cooperation feasible. Nakajima asserts that China's continentality, Korea's pensularity and Japan's insularity create cultural and civilization differences too large to bridge, making East Asian community building unrealistic.<sup>7</sup>

Skeptics, by contrast, agree with building an East Asian Economic community, but have strong doubts regarding community building beyond the economic areas of trade and finance. They are strongly skeptical with regard to the feasibility of a political and security community in East Asia. Toshio Watanabe, President of Takushoku University, also argues that East Asia community is not possible if China and Korea must institutionalize anti-Japanese sentiment to survive as a cohesive nation, which is for domestic political unity.<sup>8</sup> Watanabe, however, agrees on merit in East Asia regional free trade area.<sup>9</sup> Noboru Hatakeyama, former Vice Minister of Ministry of Economy, Trade and Industry, also argues that a community building requires that members share values and are willing to share burdens with other members. Hatakeyama argues that Japan does not share values with China and South Korea and that an East Asian community is therefore unfeasible. Hatakeyama though asserts that it is feasible to create an East Asia Free Trade Agreement (EAFTA) which does not require yielding of sovereignty.<sup>10</sup>

On the other hand, proponents of community building, with some degree of caution, see a possibility for community building in East Asia that includes the political and security fields. Hitoshi Tanaka, former Vice Minister of Ministry of Foreign Affairs and currently Senior Fellow of Japan Center for International Exchange, argues for the building of an East Asian community, but does not envisage it in the near future. Tanaka observes that Japanese foreign policy is at a crossroads sixty years after the end of the Second World War, and faces challenges of relative decline of Japan's national strength against a background of population decline. Tanaka argues that in ten to fifteen years the economic and military power of China and India will be comparable to Japan. Although their path towards the future growth may not be smooth, Tanaka observes there is no doubt that several strong countries will emerge in Asia. In that multi-polar East Asia, Japan would require a stable regional order to survive and community building would be one of the paths available to the nation. Hitoshi Tanaka also observes that it would be difficult for East Asia to aim at a value community that shares common values like skeptics but should at first aim towards a functional community achieved through functional cooperation.<sup>11</sup> Makoto Taniguchi, President of Iwate University, argues that community building in East Asia would contribute not only to the economic development of the region but also to political stability, and thus be of tremendous benefit to Japanese economic development and security. Taniguchi asserts that the development of an East Asian community into a broader Asian community would strengthen Asian identity, and this community would be comparable to NAFTA and EU.<sup>12</sup> Yoshihide Soeya, Professor of Keio University, also argues in favor of an East Asian community, and explicitly of a security community. Soeya asserts that this is the ultimate destination of East Asian community building. When a security community is created in Asia, he argues that it would absorb the functions of the Japan-US Security alliance; however, he also argues that during the process of community building it would be essential for Asia to be prepared for all possible security threats.<sup>13</sup> Takashi Shiraishi, Vice President of National Graduate Institute for Policy Studies (GRIPS), promotes functional cooperation, including cooperation in the area of non-traditional security issues, in East Asia and underscores the difference between community building in East Asia and in Europe. While Europe has built a community in the classic sense, East Asia is characterized by webs of bilateral relationships; the challenge is how to develop these bilateral relationships into a community, from webs to network. Shiraishi also identifies that

the linkage between an East Asian community and the Japan-US alliance as a major challenge in community building.

While there is a consensus across the board that the Japan-US alliance is essential in maintaining security from the perspective of traditional security issues, opinions are divided on whether regional cooperation on non-traditional security issues including terrorism, piracy and arms, narcotics and human trafficking, energy and environment, and infectious disease can benefit the region and the United States.<sup>14</sup> Proponents of community building believe that it would serve as a vehicle for the achievement of regional stability and also as a way for Japan to field more effective Asia policy, while opponents and skeptics, as indicated above, deny the possibility of community building beyond the economy.

This chapter examines the prevailing framework for regional cooperation in political and security fields in East Asia, a possible road map for East Asian political/security community against a background of changing strategic relationships in Asia, a road map for functional cooperation and functional integration, and a linkage between East Asia and the United States. It concludes by considering the challenges and opportunities for political and security cooperation and conclude with an observation whether or not the diversity of cultures, economies and political systems in the region will enable the establishment of a viable organization in East Asia.

### **East Asian Political/Security Cooperation: Reality Check**

Since the achievement of peace in Cambodia in the early 1990s, there has been no major war in East Asia. Since the end of the Cold War, compared to other parts of the world East Asia has been relatively stable and free from violent conflicts. Against this backdrop of political stability, despite the Asian financial crisis in 1997, East Asian countries have prospered economically. Smooth economic growth has encouraged stability in the region and vice versa.

However, in the early twenty-first century East Asia still carries legacy of the Cold War time confrontations. It has been suggested that if a Third World War should break out, the first shot would most likely be heard in East Asia, in particular Northeast Asia. Given the existence of potential security risks in the region, is the establishment of a political and security community feasible?

In the past half a century, peace and stability in the Asia-Pacific region has been maintained by a web of bilateral security relations with the United States, forming a hub-and-spoke architecture. These alliance relations, combined with national defense capabilities, have maintained deterrence and provided for response to potential contingencies in the region. Since the end of the Cold War bilateral alliances with the United States have evolved from a focus on a specified threat to a focus on regional security. In the post-post Cold War era non-traditional security threats such as terrorism have surged as a focus in the region. The bilateral security treaties in East Asia, in addition to their traditional role, have gained a feature of being public goods for regional security.

America's allies in the region, the "spokes," did not develop relations among themselves during the Cold War. It is only recently in the post Cold War that "spokes" have started to form a partial "wheel," as illustrated in the TCOG talks and Japan-Australia-US trilateral talks. In the area of military exercises, third countries have started to either participate in or send observers to bilateral exercises. For example, Team Challenge, held in May 2002 combined bilateral exercises between the US and Thailand (Cobra Gold), the US and Australia (Tandem Thrust) and the US and the Philippines (Balikatan); 22 countries sent observers to these exercises. China sent observers to the Cobra Gold exercises. The background to these multilateral exercises was a 2001 article entitled "From Wheel to Webs: Reconstructing Asia-Pacific Security Arrangements" by Denis Blair of CINCPAC.<sup>15</sup> The security community proposed by Blair is different from

the pluralistic security community proposed by Karl W. Deutsch.<sup>16</sup> The precondition of Deutsch's security community is the sharing of common values such as a commitment to freedom and democracy. In such a community national conflicts can be solved peacefully without resorting to military force. In contrast, Blair's proposal was to establish a security community by deepening bilateral relations and creating a network or web of alliances. His proposal was, however, not further pursued due to 9.11. Following 9.11 the United States opted for a coalition of the willing in the war against terror, which has provided support for the invasions of Afghanistan and Iraq.

Another example of the coalition of the willing is the Proliferation Security Initiative (PSI). PSI was proposed by the Bush administration in December 2002 to control the flow of weapons of mass destruction, their delivery systems and related materials to and from states and non-state actors. President Bush announced the PSI concept during his visit to Poland in May 2003 and called on countries to participate. From Asia, Japan, Australia and Singapore are participating in the PSI. In September 2003 Australia hosted the maritime interdiction exercise "Pacific Protector," and in October 2004 Japan hosted "Team Samurai 04" off Sagami Bay and Yokosuka Port. Australia, Singapore, Cambodia, the Philippines, New Zealand and Thailand participated in the latter. In PSI, principles are agreed by a series of conferences and exercises are conducted with an emphasis on preventive interdiction. Participants voluntarily participate in PSI when they share the objective. This is due to the fact that the existing arms control and disarmament negotiations at the United Nations are based on consensus which often prevents substantive progress

### ***ASEAN Regional Forum (ARF)***

During the Cold War, Asia went through the hot wars such as the Korean War and the Vietnam War, and regional security was not addressed. Since the end of the Cold War, against the backdrop of relative regional stability, regional security has come to be recognized as a viable approach.

The major considerations from the perspective of regional security are (1) whether or not threats are specified or unspecified, (2) whether threats are internal or external and (3) whether security measures are limited to military means or more comprehensive political, diplomatic or economic means. When threats are specified and external, security must be ensured by military means and by establishing alliances. On the other hand, unspecified internal threats should be responded to by preventing disputes from escalating into conflicts by means of a national and regional framework. When internal disputes develop into violent conflicts, the national/regional framework will be used to solve them peacefully. Especially when national governance is failing, multilateral regional and/or international framework is useful to settle conflicts. Regional mechanisms can also be effective in curbing and preventing both unspecified internal and external threats, i.e. non-traditional threats. In East Asia today, both specified and unspecified, internal and external threats exist, which should be addressed by military as well as cooperative security measures. Thus, in addition to the traditional alliance network, the region also needs a regional framework to deal with complex non-traditional security threats.

The ASEAN Regional Forum (ARF) is an example of such a cooperative security framework, although it does not possess means of coercion. In 1990 when Australia and Canada proposed an Asian version of the Conference on Security Cooperation in Europe (CSCE), ASEAN countries declined the idea on the grounds that the security environments of Asia and Europe were different, and the European security approach therefore did not apply to Asia. However, in 1993 the ASEAN Post-Ministerial Meeting agreed to create the ARF as a venue to discuss regional security issues. ARF Ministerial Meetings have been held annually since the first in 1994; North Korea has participated in the ARF since 2000. 23 Asian Pacific countries, or almost the entire region, and the EU currently participate in the ARF. In 2004, an ARF unit was

created in the ASEAN Secretariat to support ARF activities. In the intervals between the annual Foreign Ministers Meetings, the ARF holds Senior Officials Meetings (SOM) and Inter-sessional Group (ISG) meetings.

The ARF is not institutionalized like frameworks for cooperative security in Europe such as the Organization for Security Cooperation in Europe (OSCE). It is still a framework for discussion and does not implement actions like election monitoring, protection of minorities and field missions for peace building as the OSCE does.

At the Second ARF Ministerial Meeting held in 1995 a concept paper was adopted that indicated a road map of ARF, from phase one of confidence building measures, phase two of preventive diplomacy and phase three of approaches to conflicts. The ARF today thus functions as a venue for participants to discuss regional security issues. When the ARF was launched, some regional countries were skeptical with regard to multilateral security dialogue. The ARF therefore could not take up sensitive issues like the Spratly Islands dispute as an agenda for its meetings. Over the years, however, the ARF has helped to reduce mistrust and nurture a sense of mutual assurance among its members. After 1997 Asian financial crisis the ARF stalled somewhat, but has come to take up sensitive issues such as the Korean Peninsula as well as the Spratly Islands. Although the ARF has developed a dialogue role in the region, its effectiveness has been questioned. When it attempted to move from phase one, confidence building measures, to phase two, preventive diplomacy, China asserted that there was an overlap between confidence building and preventive diplomacy, and the ARF could not agree on moving to the preventive diplomacy phase. After some difficulties in July 2001 the Eighth ARF ministerial meeting adopted the Paper on the Concept and Principles of Preventive Diplomacy and the ARF Register of Experts/Eminent Persons. Due to Chinese pressure owing to its concern on a possible interference by the ARF members into its domestic affairs under the name of preventive diplomacy, preventive diplomacy at the ARF was defined as applicable to inter-state conflicts and not to intra-state conflicts. The ARF, however, could not make any significant progress in preventive diplomacy; it was not able to take effective measures in East Timor after the referendum for independence, and had to rely initially on multinational forces and subsequently UN peacekeeping missions. For its peace building, it had to rely on UN mission. In the recent instability caused by unsatisfied former soldiers in May 2006, East Timor has to ask the dispatch of Australian troops to recover peace and safety.

Although East Asia certainly needs more time before a pluralistic security community can be created, the ARF and ASEAN+3 despite their shortcomings can in the interim work on non-traditional transnational security issues. In Karl Deutsch's concept of a security community, the nations of the region must basically trust each other and share common values. East Asia, in conceiving its future collective security community, must start from building trust among countries in the region. As a roadmap for regional cooperation and for an eventual community building East Asian way, functional cooperation in non-traditional security fields such as counter-terrorism, piracy, energy, environment, infectious disease and drug trafficking would be productive both for trust building and for practical benefits it would generate. The growing number of transnational security threats would increasingly demand such cooperation in the region.

In preparing and planning such cooperation, political/security dialogues are necessary. When the ARF was created in 1994, opinions were divided as to whether multilateral politico-security dialogues were useful and sustainable. However, multilateral dialogues like the ARF have come to be recognized not as a substitute but as a supplement to hub-and-spoke alliance relations. The EASR announced by the US Department of Defense in 1995 also recognized that dialogues do not substitute for alliance relations or forward deployment of the United States, but rather supplement them. The 2003 Japanese Diplomatic Blue Book indicated that Japanese security policy centers on the nation's alliance with the United States but also

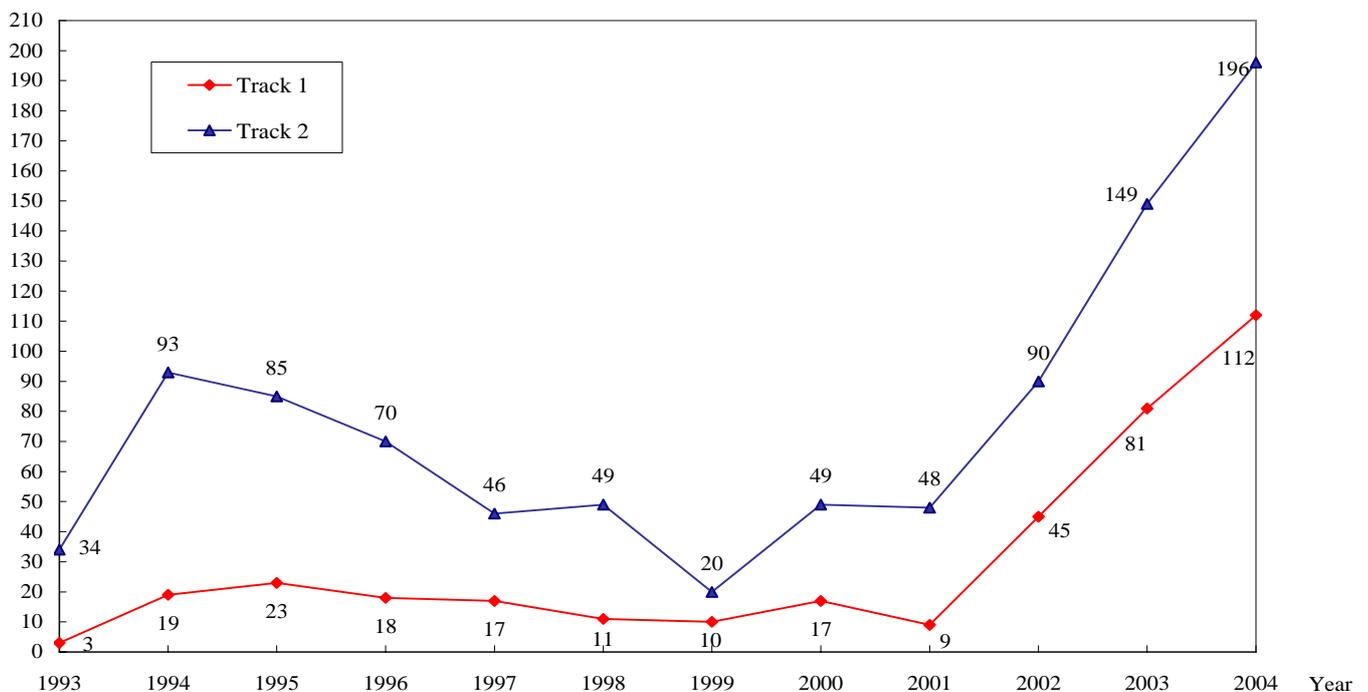
seeks to strengthen bilateral or multilateral dialogues for the peace and stability of the Asia Pacific region. However, other than ARF and ASEAN+3, there is no intergovernmental politico-security dialogue in the region specifically. What we have are track two dialogues, as described in the following section.

### Track Two Dialogues

Dialogues initiated by the private sector, generally think tanks and research institutions, are termed “track two,” as opposed to “track one” intergovernmental dialogues. Government officials may, however, participate in track two meetings in a personal capacity. This is sometimes referred to as “track one and a half.” At track two meetings, participants can float new ideas which it is perhaps too early to propose at official intergovernmental meetings, and can speak their minds in ways that they cannot in official meetings. Track two discussions can therefore help to trigger intergovernmental dialogues or prepare the groundwork for official discussions on sensitive and complex issues. Together with scholars, former government officials play an important role in track two meetings. Regional epistemic communities such as the ASEAN Institute of Strategic and International Studies (ASEAN-ISIS), the Council for Security Cooperation in the Asia-Pacific (CSCAP) have played an important ideational role in support of inter-governmental regional institutions. In the context of East Asian community building, the East Asia Vision Group (EAVG) established by ASEAN+3 and the Network of East Asian Think Tanks (NEAT) that was established on the basis of EAVG’s recommendations are good examples of track two processes.

The number of track two dialogues in the Asia Pacific region has increased since the 1990s, as shown in Figure 1. Figure 1 is based on data from the *Dialogue and Research Monitor*,<sup>17</sup> initially compiled by Canadian universities and subsequently by the Japan Center for International Exchange (JCIE). Given that the number of meetings varies depending on how they are counted, these numbers should not be considered absolute; however, they do give a good idea of trends of track one and two meetings since the 1990s.

**Figure 1: Evolution of Politico-Security Dialogues in Asia Pacific Region**



Source: Japan Center for International Exchange(JCIE) "Dialogue and Research Monitor Towards Community Building in East Asia" (<http://www.jcie.or.jp/drm/index.html>)

Figure 1 includes a variety of track two processes: bilateral and multilateral, for specified

objectives and for general exchange of views, institutionalized and ad hoc. During the 1990s the number of track two meetings in the region peaked at 93, but this figure had declined to 20 in 1999. Because the region had little experience of track two meetings in the preceding decades, they were initially organized with considerable enthusiasm; however, they were soon criticized for excessive growth and a lack of results. Jokes circulated recommending non-proliferation of track two meetings, and suggesting that CBM referred to “conference building” rather than “confidence building” measures. The decline in the number of track two meetings was further influenced by the 1997 Asian financial crisis, which deprived track two meetings of funding. During the same period of time, track one meetings have been fairly constant in terms of the number of annual meetings. However, the benefit of track two meetings as a way of deepening mutual understanding and trust has been recognized; as Figure 1 shows, the number of meetings has registered a substantial increase since 2000, reaching 196 meetings in 2004. This phenomenal growth reflects the fact that non-traditional and human security issues have been taken up at track two meetings since 9.11. The latest *Research and Dialogue Monitor* of 2005 observes that “terrorism featured in one quarter of all Track 1 meetings and proved to be the most frequently dealt with of any single issue...topics such as maritime terrorism, piracy, and cyber crimes were prevalent, particularly in Track 1, indicating the level of concern about these issues at the governmental level. Other non-traditional security issues that were important subjects of discussion included transnational crimes, especially human trafficking, drugs trafficking and arms trafficking.”<sup>18</sup> It is also worth noting that the number of track one meetings, which had been around ten or twenty at the maximum in the 1990s, grew to 112 in 2004. This is partly due to meetings convened by ASEAN+3, which can be classified as functional cooperation,<sup>19</sup> as described in the next section. Both track one and two meetings have taken up non-traditional security issues which have been increasing with greater regional interdependence and the concomitant increased flow of people and goods across national borders.

### **A Road Map for Functional Cooperation in East Asia**

Thus, because East Asia has not reached the stage of creating a pluralistic security community in Karl Deutsch’s sense, the region cannot rely on a collective security community to ensure regional security. East Asia has to remain dependent on a web of bilateral alliances with the United States. However, regional security cooperation can play the role of “peacekeeper” in East Asia. The process can be commenced from cooperation in practical areas, in which participants share common benefits, i.e. functional cooperation. In other words, given lack of trust and common threat perceptions, East Asia cannot adopt an institutional approach in promoting regional cooperation in political and security fields in immediate future. East Asia can move forward to substantive collaboration on the myriad complex issues. In hindsight, the germ of the European Union, which has reached the stage of developing a common foreign and security policy, was the creation of European Coal and Steel Community, which was nothing but functional cooperation. In fact, triggered by the financial crisis the region went through in 1997, ASEAN+3 has embarked on the creation of a network of functional cooperation in the financial area. The report of the EAVG recommended concrete functional cooperation. These recommendations were further examined and grouped into short-term and long-term goals by the inter-governmental East Asia Study Group (EASG). As short-term measures, the report recommended strengthening mechanisms for cooperation on non-traditional security issues and poverty reduction. As medium-term and long-term measures, the report recommended numerous fields including building a framework for energy policies, strategies and action plans. Incidentally, among the medium-term and long-term measures, the EAVG recommended promoting the evolution of the ASEAN+3 Summit into an East Asian Summit. The latter has been realized in December 2005 although it was not the evolution of the ASEAN+3 Summit but the simultaneous holding of the two Summits. Of the numerous

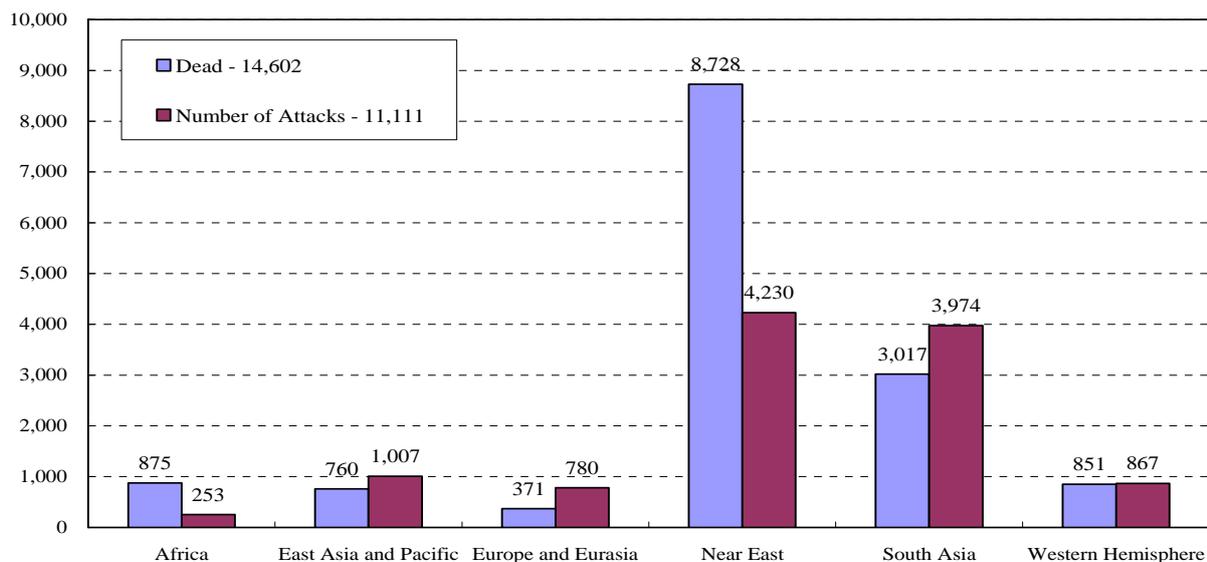
forms of functional cooperation envisaged by ASEAN+3, the next sections consider cooperation in the areas of counter-terrorism, energy, environment and piracy as illustrations.

### Counter-terrorism Cooperation

Terrorism is not a new security threat. Neither is it a particularly new phenomenon to Asia, although the current terrorist threat is clearly different from the secular communist insurgencies during the Cold War. Moreover, the scale of the 9.11 attacks and the means used in them drastically increased the perception of the security threat represented by terrorism.

Asia has its own indigenous terrorist groups, for example the MILF in the Philippines and *al-Jemaah al-Islamiyah* (JI) in Indonesia. In recent years JI, which declares its goal to be the creation of a pan-Southeast Asia Islamic caliphate has been responsible for a series of bomb attacks in the region including bomb blasts in Bali in October 2002 and October 2005, attack on the J.W.Marriott Hotel in Jakarta in August 2003 and attack outside the Australian embassy in Jakarta in September 2004. Figure 2 shows the number of terrorist attacks in 2005 by region based on data from the Report on Incidents of Terrorism published by the US National Counterterrorism Center. The combined figures for East Asia and the Pacific and South Asia are higher than for the Near East, which had the highest number in 2005.

**Figure 2: International Terrorist Attacks by Region (2005)**



Source: National Counterterrorism Center (NCTC) "Report on Incidents of Terrorism 2005" (<http://wits.nctc.gov/Reports.do>)

After 9.11, the US government launched a war against terror, regarding terrorism as a war. Although the international community was initially sympathetic with the US, opinion has since been divided over the attack on Iraq and other aspects of US policy. In Asia, Indonesia, Malaysia and South Korea have experienced a surge of anti-Americanism. Nonetheless, by contrast with Europe, most East Asian governments supported the Bush administration's war against terror. Some argued that 9.11 forced the US to take an interest in Asia again, and that terrorism in Asia can only be controlled by the United States. East Asian governments have been criticized by the citizens of their nations for their support of the US, but terrorism represents a considerable threat in the region. Moreover, the attacks in London during the G8 Summit in July 2005 were a reminder that international terrorism not only targets specific countries, but also the infrastructure and values of the civilized world.

Prevention of and countermeasures against transnational terrorism are common interests of East Asian countries. No country opposes cooperation in the area of counter-terrorism. In fact, since 9.11 existing regional frameworks have promoted concrete cooperation in this area. As an illustration ASEAN on November 4 adopted

Prevention of transnational terrorism is certainly a common interest of East Asian countries. No country opposes cooperation to counter terrorism. As terrorism is most often transnational in terms of actors and victims, regional cooperation would be effective in addition to than national measures. In fact, since 9.11 existing regional cooperation frameworks in Asia-Pacific have been promoting concrete cooperation to prevent terrorism. As an illustration, immediately after 9.11, on November 4, 2001, ASEAN adopted the Declaration on Joint Action to Counter Terrorism, which included practical measures, with ASEAN nations agreeing to “review and strengthen [...] national mechanisms to combat terrorism” and to establish “regional capacity building programmes to enhance existing capabilities of ASEAN member countries to investigate, detect, monitor and report on terrorist acts.”<sup>20</sup> ASEAN meetings have continued to condemn terrorist attacks and have suggested numerous regional cooperation initiatives for preventing and combating terrorism

The Asia Pacific Economic Cooperation (APEC) conference, despite its focus on economic cooperation, also reacted to 9.11 and has taken up international terrorism as an agenda every year since 2001. On October 21, 2001, APEC leaders, at the strong urging of the United States, declared their condemnation of and determination to respond to international terrorism.<sup>21</sup> On October 26, 2002, APEC leaders announced the Los Cabos Statement on Fighting Terrorism and Promoting Growth, declaring their commitment to blocking the financing of terrorist organizations, promoting cyber-security and cooperating in capacity building through counter-terrorism-related training.<sup>22</sup> The Los Cabos Statement led to the creation of the Counter-Terrorism Task Force (CTTF).<sup>23</sup> On 21 October, 2003, the APEC Leaders’ Statement, under the heading of “Enhancing Human Security,” declared a commitment to “dismantle, fully and without delay, transnational terrorist groups that threaten the APEC economies.” The declaration also mentioned the implementation of a Health Security Initiative to “help APEC prevent and respond to regional health threats, including naturally-occurring infectious disease and bio-terrorism,” in addition to the establishment of a “regional trade and financial security initiative within the Asian Development Bank to support projects that enhance port security, combat terrorist finance, and achieve other counter-terrorism objectives.”<sup>24</sup> With the campaign on Secure Trade in the APEC Region (STAR), APEC has cooperated in countering terrorism from the economic perspective through measures that protect cargo, ships, international aviation and people in transit and prevent money laundering. In their 18-19 November 2005 Declaration, APEC leaders made a commitment to further strengthen their efforts on counter-terrorism beyond the economy by dismantling transnational terrorist groups, eliminating the danger posed by the proliferation of weapons of mass destruction, their delivery systems and related items, and confronting other direct threats to the security of the region.<sup>25</sup> Previously, when it was proposed that security be included in the agenda, APEC participants could not reach consensus as Taiwan, which is not a country, participates in APEC, and some members resisted the idea of discussing security issues with such a participant. However, since 9.11, APEC has come to collaborate on the terrorism issue which has significant implications on economic activities.

The ARF has also condemned and responded to terrorism. The ARF issued “the Statement on Measures against Terrorist Financing,” making a commitment to freeze terrorist assets, exchange information and outreach and provide technical assistance “in developing and implementing necessary laws, regulations and policies to combat terrorist financing and money laundering.”<sup>26</sup> ARF created the Inter-sessional Meeting on Counter-Terrorism and Transnational Crime (ISM on CT-TC). At the first meeting, held in Karambunai, Sabah, Malaysia in March 2003, co-hosted by Malaysia and the United States, the adoption of the ARF

Statement on Cooperative Counter-Terrorist Actions on Border Security was proposed. In 2004 ARF ministers adopted the ARF Statement on Strengthening Transport Security against International Terrorism, and agreed to review its implementation every year.<sup>27</sup>

East Asian countries have held numerous meetings on counter-terrorism issues which have contributed to the growth of track one meetings and have held intensive discussions under existing regional frameworks to combat terrorism since 2001; they have also embarked on improving law enforcement programs and operations, disrupting terrorist financing, capacity building on intelligence collection, analysis, distribution and exchange, and the enhancement of global commitments in the region. In Malaysia the Southeast Asia Regional Centre for Counter-Terrorism (SEARCCT) has been established to conduct training to counter terrorism. East Asian countries share a practical interest in preventing and responding to terrorism, due to the practical benefits of doing so.

### ***Maritime Cooperation: Fighting against Piracy***

The Straits of Malacca extends approximately 900 kilometers; 80,000 vessels cross it a year, including numerous oil tankers transporting crude oil from the Middle East to East Asia. Due to the economic growth of East Asia, the number of ships crossing the Straits of Malacca has increased significantly, and the quantity of oil transported is growing every year. According to Institute of Defence and Strategic Studies based in Singapore around 30 percent of world trade and 50 percent of world energy needs pass through the Straits each year.<sup>28</sup> However, ships in the Straits are the targets of pirate attacks. It is also reported that piracy has become more violent in recent years. Pirates are now armed with stronger weapons such as AK47 assault rifles and even rocket launchers.

In March 2005, the Japanese tug boat *Idaten* was attacked by pirates during a voyage through the Straits of Malacca. Its crew were taken hostage, but later returned to Japan. The case sent a message home once again that the Straits of Malacca is prone to piracy.

According to International Maritime Organization (IMO) statistics, the South China Sea and the Straits of Malacca record a high incidence of piracy, as shown in Table 1. The combined incidence of piracy in these two areas gives East Asia the highest incidence of piracy in the world. Because of this high incidence, functional cooperation to combat the problem is already underway. Thus, due to multilateral strict control measures the number of incidents of piracy and armed robbery against ships in the Straits of Malacca which reached 112 in 2000 has reduced to ten in 2005. After Tsunami off Sumatra and Indian Ocean in December 2004, incidence of piracy has declined which is reflected in the figures in Table 1. It was analyzed

Table 1: Piracy and Armed Robbery against Ships

	1998	2000	2002	2003	2004	2005
Malacca Strait	6	112	24	15	35	10
South China Sea	94	140	112	114	86	81
Indian Ocean	25	109	46	77	31	39
East Africa	19	29	14	11	7	22
West Africa	22	33	39	59	43	21
South America	38	41	53	60	40	24
Mediterranean Sea	2	2	3	1	-	-

Source: International Maritime Organization (IMO) "Report on Acts of Piracy and Armed Robbery against Ships Annual report ", regional analysis of reports on acts of piracy and armed robbery against ships which were reported to have been allegedly committed (<http://www.imo.org/HOME.html>)

that pirates themselves were hit by tsunami and could not act. Moreover pirates are afraid of relief ships which led them to be cautious. However, they have started to be active again because economy has recovered from Tsunami damage and ships which are targets of piracy have resumed their voyage. There is therefore no room for complacency on piracy.

Why are there so many pirates in the region? According to Yoshihiko Yamada of the Nippon Foundation, when the Kingdom of Malacca became a colony of Portugal in 1511, Malaccans resisting the colonization fled to islands on the Indonesian side and earned their living by fishing. However, seeking more income in addition to fishing and sometimes as resistance to imperial powers, they became pirates.<sup>29</sup>

Pirates have aimed at cargoes and ships themselves in the past. The ships seized have been repainted in unpopulated harbors and their names are changed, after which they are used in acts of piracy. Cargoes are sold on the black market. Petroleum products, particularly refined gasoline and kerosene, which have high added value, have been specific targets of piracy. Recently although sea robbery remains to be the most common type of attack, pirates are increasingly going after kidnap-for-ransom. Thus, it is a recent trend to hijack smaller vessels rather than larger vessels. Since pirates are after ransom, they attack smaller tankers and tug boats which are slow in their speeds and easier to board and seize than larger boats.

The trigger for regional cooperation against piracy in East Asia was the Alondra Rainbow incident. This Panama-registered ship was owned by Imura Kisen in Imabari City, Ehime Prefecture, Japan. When attacked by pirates in October 1999, the boat was on loan to Tokyo Senpaku and manned by a Japanese captain and chief engineer and fifteen Filipino crewmen. On October 22 1999, the ship loaded 7000 tons of aluminum ingots at an Indonesian port and departed for Miike port in Fukuoka Prefecture. However, soon after its departure from Indonesia, contact with the ship was lost. It was attacked by pirates in the Straits of Malacca and the entire crew was forced to board another ship. The Alondra Rainbow was taken to Sarawak, Malaysia, repainted and given the new name of Global Venture; it was later seized by the Indian coast guard. The search for the ship and the investigation of the case involved eight countries, clearly indicating that regional cooperation is absolutely necessary for countering piracy. For example, when a vessel is in Indonesia's jurisdiction, the Malaysian authorities cannot pursue it and vice versa, which impedes the pursuit and arrest of pirates. Action against piracy clearly requires transnational cooperation to be effective and efficient.

Given the need of regional cooperation to deter and respond to piracy, the late Japanese Prime Minister Keizo Obuchi thus proposed an international conference to combat piracy in the region at the ASEAN+3 Summit Meeting on November 28, 1999. In April 2000 his proposal was realized. Japan hosted the Regional Conference on Combating Piracy and Armed Robbery against Ships involving coast guard agencies and maritime policy authorities in East Asia. The conference produced an outline of piracy measures for Asian countries to forge partnerships in implementing. Since then Asia Regional Experts' Meeting on Piracy has been held every year.

Sovereignty and different national priorities have, however, been obstacles to cooperation, not allowing "hot pursuit." In the case of the Idate, Malaysia, Indonesia and Singapore have been conducting a joint patrol, but the three countries did not share the information that the vessel used by the pirates was a stolen boat. Collaboration after the attack was also reported as insufficient, due to the complexity of territorial issues in the straits. As it involves sovereignty of the littoral states, the dispatch of coast guard vessels is decided by each county.

In November 2004 ASEAN, China, India, Sri Lanka, Bangladesh and Japan negotiated the Regional Cooperation Agreement on Combating Piracy and Armed Robbery against Ships in Asia, which, once ratified, will be a legal framework for regional cooperation. An information center has also been

established in Singapore for sharing of information on piracy. Functional cooperation is thus already underway against piracy. It is worth noting that anti-piracy measures are being promoted not by naval cooperation but by coast guards. Countries that do not possess coast guards are creating them, as in the case of Malaysia and Indonesia. Anti-piracy cooperation, however, faces the challenge of surmounting the question of jurisdiction among countries in the region which prevents pursuit and other effective control measures. Pirates are transnational in their activities and control measures must therefore also be transnational. However, police agencies and coast guards cannot exercise their powers beyond national borders. Pirates are taking advantage of these limitations and are escaping.

In addition to piracy there are other potential threats on the sea, including terrorism. East Asia needs to develop a scheme whereby maritime security including sea lanes of communication (SLOCs) can be ensured without infringing sovereignty and jurisdictional limits. Maritime security is so closely tied to economic and energy security of East Asia as described in the following section. Sea lanes of communication constitute the lifeline of East Asian economies reliant on energy from other regions and on exports to others.

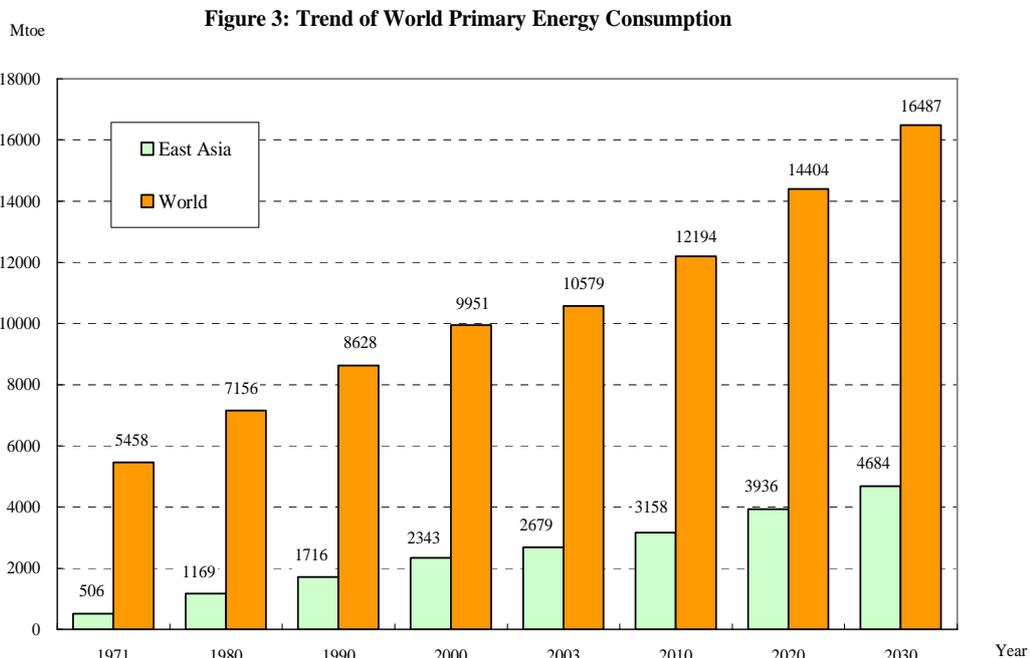
### ***Energy Cooperation***

The need to secure an energy supply has at times acted as a causative factor of war. The pursuit of oil resources was one of the reasons for Japan's expansion into Asia and attack on the Allied powers more than half a century ago. Following the occupation of southern Indochina by Japanese troops in June 1941, the US, the UK and the Netherlands froze Japanese assets, ensuring that the nation, which does not possess significant indigenous oil resources, was unable to purchase oil. Japan therefore made plans to gain access to oil resources in Southeast Asia, leading to the attack on Pearl Harbor and the seizing of Indonesian oil fields owned by the Dutch East India Company by Japanese paratroop units. Energy has therefore been directly related to security.

In hindsight, functional cooperation on energy in the form of the creation of the European Coal and Steel Community after World War II was the commencement of the process of European integration. The intention behind this initiative was to prevent a third world war by controlling coal and steel, which are essential materials for warfare. Energy security was the main agenda during the oil crisis in 1970s, and has once again emerged as a common topic in the region in the twenty-first century, against a background of spiraling oil prices. Energy has been politicized. Some resource rich countries have opted to limit FDI and to nationalize energy related companies. Some buyers on the other hand have opted to buy up resources overseas. Energy security has two facets; at the macro level energy security means competition for natural fossil fuels and is a national security issue with geopolitical and geo-economic aspects, as demonstrated by the fact that energy supply can be a factor in causing war and territorial disputes. At the micro-level, energy security is a question of how energy supply is secured, including sea lane security. At the latter level, energy cooperation has been explored since the 1990s in Asia, in particular in Northeast Asia. This is due to the fact that energy demand in Asia has increased significantly due to the phenomenal economic growth of the region. Some former oil exporters, including China, have become oil importers. Since the 1990s, proposals have been made for the creation of a Northeast Asian Energy Community, in which resource-rich countries like Russia and the Central Asian states and resource-poor but financially rich and technologically advanced countries like Japan and Korea cooperate in a variety of ways, including the construction of oil and gas pipelines. Energy cooperation has long been identified as the most promising form of functional cooperation for the region since 1990s, but the proposals have remained at the stage of discussion. This is because of low crude oil prices in the past 15 years and competition between oil consuming countries over bilateral trade with oil producing countries, a situation that has not been conducive to multilateral cooperation in oil and

gas import.

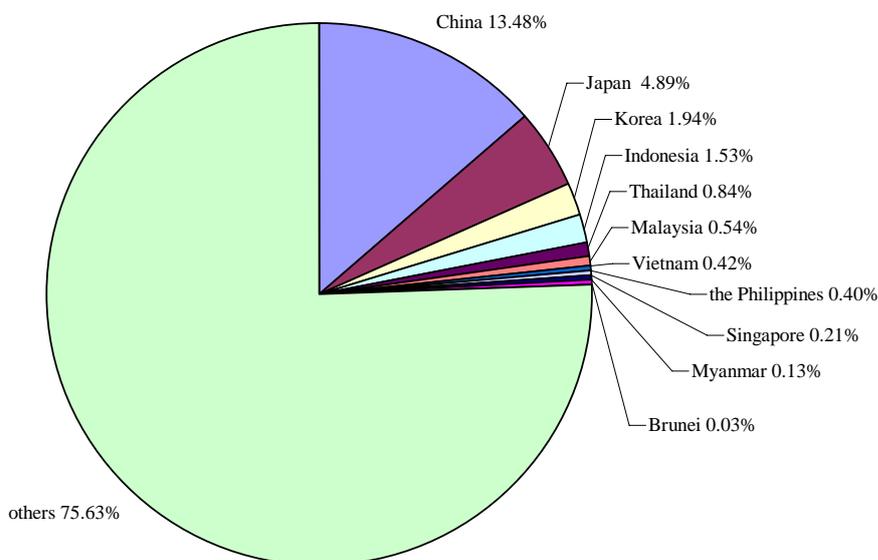
Both the EAVG and the EASG also recommended functional cooperation on energy within the framework of ASEAN+3. The ASEAN+3 Energy Ministers' Meeting has been held since 2004. APEC also organized a working group on energy cooperation and has promoted dialogues among member countries. With higher oil prices, the oil demand and supply situation in the region is making energy cooperation more mutually beneficial than ever.



Source: International Energy Agency (IEA), *Energy Balances of OECD Countries 2002-2003: 2005 Edition*, *Energy Balances of Non-OECD Countries 2002-2003: 2005 Edition*, and *World Energy Outlook 2004*

Note: East Asia in the projection of 2010, 2020 and 2030 includes Japan, Korea, China and the following countries according to the OECD's regional definition: Afghanistan, Bhutan, Brunei, Chinese Taipei, Fiji, French Polynesia, Indonesia, Kiribati, Democratic People's Republic of Korea, Malaysia, Maldives, Myanmar, New Caledonia, Papua New Guinea, the Philippines, Samoa, Singapore, Solomon Islands, Thailand, Vietnam and Vanuatu.

**Figure 4: Share of East Asia in World Primary Energy Consumption (2003)**



Source: International Energy Agency (IEA), *Energy Balances of OECD Countries 2002-2003: 2005 Edition*, *Energy Balances of Non-OECD Countries 2002-2003: 2005 Edition*, and *World Energy Outlook 2004*

In addition to soaring energy prices, East Asia has more consumers than producers of primary energy. According to the International Energy Agency (IEA) of the OECD, world primary energy consumption will increase by 2.1 percent per annum from 2000 to 2030, as shown in Figure 3. Compared to figures for 1971, Asia's primary energy consumption has increased five-fold while overall world consumption has increased only two-fold. As shown in Figure 4, Asia's share of world energy consumption increased from 9.3 percent in 1971 to 24.4 percent in 2003, and is predicted to reach 28.4 percent in 2030. In terms of increase from 1971, Malaysia and Thailand have increased their consumption by eight times, Indonesia and Korea by five times, China by three times and Japan by two times. China now consumes more energy than Japan. Excluding Japan the increase of primary energy consumption in East Asia due to economic growth has been phenomenal, greater than that observed in any other region.

Particularly China's oil consumption has grown due to its economic growth, its low energy efficiency, increasing automobile ownership and surging petrochemical production. Since 1990 the number of automobiles registered in China has risen roughly twenty-fold. China is the fastest growing automobile market in the world. With five million car sales in 2004, it is already the world's third largest car market, and *The Economist* predicts that it will become the largest between 2010 and 2015. Almost all of China's automobiles will use oil-based fuels, and virtually all of the oil required will come from imports. China's oil consumption passed Japan's in 2002, and the nation became the second largest consumer in the world after the United States. According to the IEA forecast, Chinese oil imports will grow from the current 2 million barrels a day to 10 million barrels a day in 2030. Although China is still the world's fifth largest oil producer, continuing to draw on large fields in the northeast, such as Daqing, environmental and infrastructural problems and the nation's reluctance to offer incentives for foreign investment in oil development make it unlikely that China will produce significantly more oil in future. In addition, again according to IEA statistics, East Asia's intraregional oil production in 2002 was 308 million tons, which represents only 8.4 percent of the world total. It is predicted that other oil producing nations in the region, such as Indonesia and Vietnam, will reduce production from 2010 unless they discover new reserves. Indonesia has not conducted new oil exploration, and had to reduce its gasoline supply by 5 percent in 2005. Declining oil reserves are also affecting electricity supply in the country.

This imbalance between demand and supply of oil in East Asia may become an Achilles' heel for economic development and stability of the region. Moreover, East Asia depends heavily on Middle Eastern oil. According to IEA data, dependence on Middle Eastern oil in 2003 was 87.1 percent for Japan, 79.8 percent for Korea, and 50.9 percent for China. Oil stockpiling is not well-developed in East Asia, and if supply from the Middle East should be disrupted for some reason, it may have a major effect on economic activity in the region. In addition, the oil import route from the Middle East involves a long and dangerous sea route termed an "arc of instability," including the Strait of Malacca.

Thus, demand for oil in East Asia is growing and intra-regional supply is on the decline, and this may lead to competition over drilling rights for oil and gas, including offshore rights. The Sino-Japanese dispute in the East China Sea is one such example. In East Asia, a shortage or disruption of oil supply would undermine energy security both at the macro and micro level. East Asia has numerous reasons to identify common interests and promote functional cooperation in the area of energy.

First and foremost, stable energy supply should be achieved not by competition but by cooperation. An oil pipeline from Russia to East Asia, in particular to China, South Korea and Japan, would be an option to consider. It is reported when Russia develops untapped oil and gas resources particularly in its Far East, the world supply and demand would improve. The region must also work on geographical diversification of its energy supply. Meanwhile, the region must make collective efforts to secure sea lanes for the

transportation of oil, given its high level of reliance on Middle Eastern oil.

Secondly the region should also seek improved energy efficiency. Improvement in energy efficiency is said to be worth a major discovery of a reservoir. China has already implemented efforts to better energy efficiency. In 1993, China's energy efficiency was one-twentieth Japan's, but that figure has now been reduced to one-seventh. In July 2005, China began to introduce automobile fuel efficiency standards that require new cars to achieve up to two miles more per gallon. The introduction of a fuel tax is also being considered in China. The nation has also started to work on the achievement of increased energy efficiency in industry. It is claimed that increased energy efficiency can reduce consumption in China by 30-40 percent. Japanese companies have started their cooperation to China for example in steel making to improve their energy efficiency.

Thirdly, the development of an oil stockpile that can be used in case of emergency by creating an Asian version of IEA has been proposed. East Asia must diversify its energy supply towards nuclear power, hydroelectric power and natural gas. There is currently no natural gas pipeline in the region. Supply of gas by pipeline to Japan, Korea and China from the abundant reserves in Eastern Siberia has been proposed.<sup>30</sup> This long-standing proposal now has a greater economic incentive than ever, given the higher prices of oil. Such transnational pipeline will have significance not only for energy supply but also for regional security.

Fourthly, the region should also attempt to develop new, alternative and renewable energies such as nuclear power, solar power, wind power, bio-fuel etc. Collective development projects and sharing of information would prevent the duplication of effort in this area.

Numerous regional energy initiatives have been proposed or are currently underway; ASEAN+3 has launched ASEAN+3 Ministers on Energy Meeting since 2004 with one of the ASEAN countries serves as co-chair in alphabetical order and one of the +3 countries serves as co-chair. ASEAN+3 SOM has also launched an annual meeting on energy in 2002 by the Japan's proposal to discuss common issues. They have also created Biomass-Asia Workshop which is an annual event involving Asian countries which use biomass. East Asia would benefit from combining these initiatives under a regional framework. Regional cooperation should be linked to global initiatives, including the Joint Oil Data initiative, in which many Asian countries are participating. Functional cooperation on energy can offer visible benefits for participants and has a potential for a good model case for cooperation when designed well. With skyrocketing oil prices, energy cooperation is more promising than the preceding decade.

### ***Environment Cooperation***

The other side of the coin of energy consumption is pollution which is Tran boundary in nature, including global warming and climate change caused by carbon dioxide (CO<sub>2</sub>) and other greenhouse gases. The depletion of biodiversity and the issue of disposal of hazardous materials also represent environmental problems. Because pollution spreads via air and water, its impact is not contained by national borders but extends to neighboring countries and entire regions. Environmental issues thus demand collective measures. Given East Asia's phenomenal economic growth, balancing environmental protection and economic growth is an increasingly important policy agenda. Environmental issues must be approached by global measures but be augmented by regional measures particularly in East Asia.

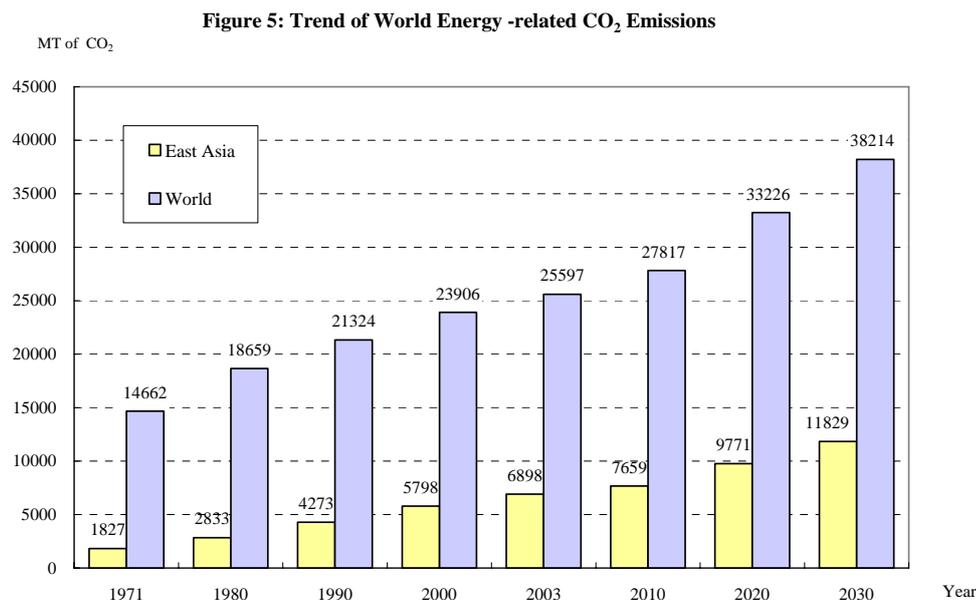
The region's reliance on coal has, for example, produced sulfur dioxide emission causing acid rain, air pollution and smog. China's increasing coal consumption has increased the load on the environment which has generated numerous problems for neighboring countries. East Asia needs to coordinate its environmental policies, take collective steps and establish common environmental standards to mitigate the problem of pollution in the region.

Being aware that environmental issues have at times led to regional disputes, the EAVG proposed “the establishment of a comprehensive East Asian environmental cooperative body which includes a dispute settlement mechanism and a regional environmental database”<sup>31</sup> and also that “an East Asian Environment Ministers’ Meeting be organized periodically for the coordination of regional environmental projects.”<sup>32</sup> While the former has yet to be implemented, the latter proposal has already been realized. ASEAN+3 Environment Ministers’ Meeting was launched in 2002 by the proposal of ASEAN Ministerial Meeting on the Environment which has been meeting since 1981. The meeting has identified ten priority areas; namely (1) global environment, (2) forest fires and cross-border haze, (3) coastal and marine environment, (4) sustainable forest management, (5) sustainable management of natural parks and reserves, (6) freshwater resources, (7) environmental education, (7) promotion of environmentally suitable technology and cleaner production, (9) urban environment management and governance, and (10) harmonized monitoring, reporting and database for sustainable development. In addition, the Tripartite Environment Ministers Meeting among Japan, China and Korea (TEMM) has been held since 2000.

Although these inter-governmental meetings have not yet produced joint projects, awareness of the importance of environmental conservation has increased in East Asia, prompting the region to work on the reduction of air pollution in particular. With consumption of fossil fuels projected to increase in future, it will be essential to enhance environmental standards. As air pollution and acid rain influence health in the short term, the incentives for adopting the necessary measures are clear, and East Asian nations have already started to introduce, de-NO<sub>x</sub> and de-SO<sub>x</sub> equipment.

The effects of global warming, by contrast, are generated over the long term. The phenomena of desertification and climate change associated with global warming occur so gradually that they do not motivate actors to take immediate countermeasures. However, CO<sub>2</sub> emissions in East Asia are certainly increasing, and action needs to be taken now to avoid future environmental problems.

As shown in Figure 5, worldwide energy-related CO<sub>2</sub> emissions increased approximately 2.5-fold from 1971 to 2003 while CO<sub>2</sub> emissions in East Asia increased approximately six-fold due to the region’s high consumption of coal. East Asia’s CO<sub>2</sub> emissions represented 12.5 percent of the world total in 1971, but this figure had increased to 27 percent in 2003.



Source: International Energy Agency (IEA), *CO<sub>2</sub> Emissions from Fuel Combustion 1971-2003: 2005 Edition* and *World Energy Outlook 2004*

Note: East Asia in the projection of 2010, 2020 and 2030 includes Japan, Korea, China and the following countries according to the OECD’s regional definition: Afghanistan, Bhutan, Brunei, Chinese Taipei, Fiji, French Polynesia, Indonesia, Kiribati, Democratic People’s Republic of Korea, Malaysia, Maldives, Myanmar, New Caledonia, Papua New Guinea, the Philippines, Samoa, Singapore, Solomon Islands, Thailand, Vietnam and Vanuatu.

CO<sub>2</sub> emissions increased approximately 1.5-fold in Japan, four-fold in China, five-fold in Vietnam, eight-fold in South Korea and Singapore, ten-fold in Malaysia and Thailand and twelve-fold in Indonesia. It is clear that East Asia must reduce its carbon dioxide emissions to halt any further degradation of the environment.

The Kyoto Protocol took effect in February 2005. The Protocol was an epoch-making step towards mitigating global warming. However, it entails problems. Major CO<sub>2</sub> emitters like the United States and China have not ratified the Protocol. Moreover, the Protocol does not oblige developing countries to reduce their carbon dioxide emissions. Emissions by the countries that have committed to the Protocol represent only 30 percent of world total CO<sub>2</sub> emissions. Even when these countries reduce their emissions as required by the Protocol, it will only reduce world emissions by two percent. This will represent only a marginal improvement.

The Kyoto Protocol provides for three measures to supplement emission reduction efforts and to achieve reduction targets, namely Joint Implementation, the Clean Development Mechanism and emissions trading. The Clean Development Mechanism (CDM) offers the possibility of regional cooperation. If East Asia utilizes the CDM and developed countries in the region cooperate with developing countries to reduce their emissions of greenhouse gases, it would lead to further transfer of environmental technology. Developed countries in return would receive CO<sub>2</sub> emission credits that could be used towards the achievement of numerical targets required by the Kyoto Protocol. As an illustration, if Japan implemented a CDM project in China, in addition to Japan receiving credit, Chinese emissions of greenhouse gases would be reduced, thus reducing air pollution. The benefits are mutual.

CDM is a mechanism enabling environmental problems to be ameliorated as economic development is promoted. However, CDM procedures are cumbersome, and only few projects have to date been approved. Cooperation will be required to increase the user-friendliness of CDM. If more countries can effectively use CDM in global warming measures, it would have a positive influence on post-Kyoto Protocol framework consultations.

Regional cooperation on the environment in East Asia has mainly been limited to conferences as described above. Moreover, actual cooperation is still at the level of bilateral or sub-regional cooperation. Japan for example has concluded a bilateral Agreement of Cooperation for Environmental Protection with China in 1994 and Japan-China Environmental Cooperation for Twenty-first Century in 1997. The latter has led to action such as to rebuild model cities for environmental protection namely Chong Quing, Dalian and Guiyang and to build a computer network to gather and disseminate environment-related information. Southeast Asia has suffered from haze due to forest fires in Sumatra and Kalimantan, leading to a Southeast Asian action plan on transnational haze pollution And the introduction of regional monitoring and emergency measures on forest fires.

The Asia-Pacific Partnership on Clean Development and Climate,<sup>33</sup> involving Australia, China, India, Japan, South Korea and the United States, is also underway. This was originally proposed by President Bush to substitute for US non-ratification of the Kyoto Protocol. This Partnership involves voluntary practical measures taken by these six countries in the Asia-Pacific region to create new investment opportunities, build local capacity and reduce barriers to the introduction of clean, more efficient technologies. .

Yellow dust is another trans-boundary pollutant from China, reaching Korea and Japan. In future, these bilateral and sub-regional or voluntary environmental initiatives should be developed into a combined regional framework for environmental cooperation. With post-Kyoto Protocol frameworks being considered, it is essential to establish measures for incentives for developing countries to take part in environmental

conservation efforts. Environmental issues should be approached collectively and have the potential to enable viable regional functional cooperation like in the case of energy cooperation.

### **Functional Cooperation leading to Functional Integration?**

Will these initiatives for functional cooperation on terrorism, energy, environment, piracy and infectious disease lead to the functional integration of East Asia? Will functional cooperation lead to functional integration? As described in the preceding section, it seems the region is heading for multiple overlapping schemes for functional cooperation sometimes involving different members. Skeptics regarding East Asian community building argue that functional cooperation will not lead to regional community unless the region comes to embrace a common vision and values. Nonetheless, it is too early to indicate that functional cooperation will not lead to integration of any sort in East Asia. If East Asia develops a sense of regional partnership through functional cooperation, it is plausible that the region will express a common political will. Regional collective measures in functional areas would certainly contribute to global issues as well. For example, against a backdrop of soaring energy prices and increased demand, East Asia may have more opportunities to influence global energy policy by acting as a region.

East Asia still has flashpoints and is not likely to create a politico-security community with substantive unit of power at any time soon. It is impossible for East Asia to substitute the hub and spoke bilateral alliance architecture with a community, but it can supplement web of alliance structures. Functional cooperation on political and security would focus mainly on non-traditional security issues while the region embraces hard security issues. The purpose of such cooperation would thus be to mitigate political confrontation and to enhance stability in East Asia, that is, to keep the peace. Whether political and security cooperation in East Asia leads to community building depends on the region's future efforts. Very skillful architects are required to promote political and security cooperation in the region.

This cooperation also needs eventually to be buttressed by common values and visions. The Policy Report of the CEAC in 2005 states that “ The Community's ideals must envisage mutual security within a security community (no-war community), promote prosperity founded on a balance between economic competition and cooperation and ensure a community of progress dedicated to such values as freedom, democracy and respect for human rights.”<sup>34</sup>

### ***Linking East Asia Community with the United States***

Promotion of the East Asian community concept has to be considered in terms of its implications for Japan's relations with the United States, which represent the basic pillar of Japanese diplomacy. The alliance was the only realistic security option for Japan during the Cold War, considering the threat emanating from the Soviet Union. After the end of the Cold War and the collapse of the Soviet Union, the necessity for the Japan-US alliance was questioned. A rape incident involving American soldiers in Okinawa in June 1995 posed a further question on the need of the US troops in Japan. However, with the test launch of Nodon missiles by North Korea and with the Joint Declaration on Japan US security, the alliance has gained new momentum and has been strengthened. The Japanese government released the new National Defense Planning Guidelines (NDPG) in December 2004 based on the recommendations of the Council on Security and Defense Capabilities, the so-called Araki report. The NDPG stated that the objectives of Japanese security policy is to prevent any threat from directly reaching Japan and to reduce the chances of any threat arising in various parts of the world in order to prevent it from reaching Japan. The Guidelines stated that Japan will achieve these objectives through its own defense preparedness, its alliance with the United States and cooperation with the international community. Thus, the Japanese government envisions the Japan-US

alliance as a foundation of its security and defense policy. On its part, the United States has deployed 100,000 troops in the Far East and 45,000 troops in Japan as a forward deployment. This forward deployment is now being reviewed as a part of a transformation of the global deployment of US forces. The alliance has been serving two purposes; one is defense of Japan and the other is the peace and stability of Asia-Pacific. In the Joint Statement of United-States-Japan Security Consultative Committee, so-called 2+2, issued on May 1, 2006 confirmed this point by stating that “The U.S.-Japan Alliance ... is the indispensable foundation of Japan’s security and of peace and stability in the Asia-Pacific region.” It also stated that realignment “will lead to a new phase in alliance cooperation and strengthened alliance capabilities in the region.”<sup>35</sup>

Some in the United States have argued that the East Asian community concept is a framework to exclude the United States from Asia and an attempt by China to lead regional integration. In Japan many argue strongly that the presence of the United States is essential for the stability of East Asia and a community concept without the United States is simply laughable. Others argue that Japan is overly reliant on the United States, and that the creation of regional communities such as the EU and NAFTA is the trend of the times.

Certainly the United States has been an important market for East Asian countries, which have depended on export-led economic growth. Even in the post-Cold War and post-post Cold War eras, the United States is the stabilizer of a security environment which continues to be uncertain and unpredictable. As mentioned above, there is an argument to the effect that the Japan-US alliance should be further enhanced rather than instituting security cooperation in the region.<sup>36</sup> The argument should not be a simple discussion of whether to exclude or include the United States. One should remember that Europe has the EU for its regional economy and NATO for its security, the latter of which surely include the United States. Likewise, the regional economy and security in East Asia should be considered in a flexible manner. East Asia requires the presence and engagement of the United States. Simultaneously, the alliance network should not negate functional cooperation in East Asia and in this respect also the United States would in certain areas be an essential partner of East Asian functional cooperation. This approach from East Asia would help to keep the United States engaged in multilateralism in Asia despite its orientation towards unilateralism and isolationism.

At the same time, an East Asia community should be an open one. There are other regional frameworks such as APEC and the ARF. Regional cooperation in East Asia should be linked to these Asia Pacific institutions. In so doing it would be essential to revitalize these existing regional institutions. The ARF has been in a stalemate, and should be rehabilitated so that it can be linked to East Asian efforts. This would be the best way to link East Asia and the United States. An active linkage would benefit both. It is incumbent upon the United States and East Asia to revitalize these existing institutions in exploring functional cooperation.

## **In Concluding**

East Asian linkages are still less institutionalized. Yet trans-boundary non-traditional security issues introduced in this Chapter, from counter-terrorism, piracy, energy to environment demands the region to work collectively for their individual and regional benefits. The region’s emerging connections have, however, hardly displaced national interest and national identity if not nationalism. The region has lacked motivations and incentives for ties across the region. National pull has overwhelmed regional pull. National sentiments remain conspicuously strong. It appears that the achievement of a political and security community in East Asia represents a more difficult goal than the achievement of an economic community. It

has been argued that the politico-security area is the Achilles heel of an East Asian community concept.<sup>37</sup> In this there is a consensus among commentators, no matter what their position regarding East Asian community building is.

However, for the peace, stability and prosperity of East Asia, proactive efforts should not be limited to economic regional integration or regional free trade areas, but should aim at an eventual comprehensive community or partnership including political and security areas. ASEAN proposed a Security Community of its own in October 2003 at the time of the ASEAN Summit. A road map for building a security community is being discussed, but the road has turned out to be rocky, as exemplified by the aborted agreement for creating peacekeeping forces in ASEAN. Such efforts should not be limited to Southeast Asia. Northeast Asia should also work on its own regionalism to balance East Asia perhaps as an extension of Six-party talks on North Korean nuclear development to non-traditional security issues. Energy and environment cooperation introduced in this Chapter has attracted numerous proposals for sub-regional cooperation in Northeast Asia. Security and economy are linked. Peace enhances economic growth and stability and vice versa. Instead of declaring an East Asian politico-security community impossible, functional cooperation on non-traditional security issues should be given a chance. Meanwhile, we should explore whether we can extend functional cooperation to community building, with the political objective of creating a community without war. This would produce by-products. The vision making would compel Japan and countries in East Asia to conceive their respective Asia policies. When the immediate Korean Peninsula and Taiwan Strait issues are settled, an opportunity will emerge to create a collective security community in East Asia. Functional cooperation can at least pave the ground for such discussion to take place when time comes. Furthermore, multilateralism can sometimes ease bilateral frictions and tensions by offering venue for bilateral contacts.

The achievement of a community without war can be a strong common vision for East Asia. None in the region can disagree to a vision of this sort. Despite many obstacles, it might be worth while to create the backbone of an East Asian community by examining the limits and potential of political and security cooperation in East Asia. Functional cooperation on non-traditional security threats introduced in this Chapter can offer experiences for regional countries to harvest merits of working together.

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<sup>2</sup> Office of the Secretary of Defense, *Annual Report to Congress: Military Power of the People's Republic of China 2006*, 1.

<sup>3</sup> ASEAN Secretariat, "Joint Statement on East Asian Cooperation," 28 November 1999, <http://www.aseansec.org/2051.htm>.

<sup>4</sup> "Higashiajia Kyodotai ni Hantai [My Opposition to East Asian Community]," *Asahi Shimbun*, May 1, 2005.

<sup>5</sup> Naoki Tanaka, <http://www.21ppi.org/japanese/hitokoto/tanaka215.html>

<sup>6</sup> Taro Yamamoto, "Chugoku no Higashiajia Kyodotai Sakubo ni noruna [Don't Play Along with China's Schemes for East Asian Community]," *Sankei Shimbun*, December 22, 2005

<sup>7</sup> Mineo Nakajima, "Higashiajia Kyodotai ha Genjituron nanoka?" *Sankei Shimbun*, August 1, 2005.

<sup>8</sup> Toshio Watanabe, "Higashi ajia kyodotai ha seiritsu suruka [Can East Asia community be built?]" in *Nihon no Higashi Ajia Senryaku [Japan's Policy towards East Asian Economic Integration]*, Toyo Keizai Shinposha, 2005, 207.

<sup>9</sup> *Ibid.*, 218

<sup>10</sup> Noboru Hatakeyama, "Higashiajia Kyodotai no Genso wo Suteyo [Give up the Fantasy of East Asian Community]," *Chuokoron*, September 2005, 154-161.

<sup>11</sup> Hitoshi Tanaka, "21seiki Nihongaiko no Senryakuteki Kadai [Strategic Issues for 21<sup>st</sup> Century Japanese Diplomacy]," *Gaiko Forum*, No.207, (October 2005), 8-13.

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<sup>13</sup> Yoshihide Soeya, “Higashi Ajia Kyodotai Tenbo to Kadai: Kyuukyoku wa Anzen Hoshō Kyodotai [East Asian Community: Problems and Prospects – A Security Community is the Ultimate Goal],” *Nihon Keizai Shimbun*, November 28, 2005.

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<sup>15</sup> Denis C. Blair and John T. Hanley Jr., “From Wheels to Webs: Reconstructing Asia-Pacific Security Arrangements,” *The Washington Quarterly*, vol.24, no.1, Winter 2001.

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<sup>18</sup> Japan Center for International Exchange, *Dialogue and Research Monitor: Towards Community Building in East Asia*, Vol 3 July-December 2004, iv.

<sup>19</sup> “Database on the Functional Cooperation Progressing in the ASEAN+3 and Other Regional Frameworks in East Asia,” compiled by Government of Japan in June 2005 shows 48 regional frameworks by ASEAN+3 for functional cooperation.

<sup>20</sup> ASEAN Secretariat, <http://www.aseansec.org/5620.htm>

<sup>21</sup> APEC secretariat, 2001 APEC Economic Leaders’ Declaration: Meeting New Challenges in the New Century, Shanghai, China, 21 October 2001, [http://www.apecsec.org.sg/apec/leaders\\_declarations/2001.html](http://www.apecsec.org.sg/apec/leaders_declarations/2001.html)

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<sup>30</sup> <http://nagpf.org>

<sup>31</sup> East Asia Vision Group Report 2001, *Towards an East Asian Community: Region of Peace, Prosperity and Progress* Paragraph 73.,

<sup>32</sup> *ibid.*, paragraph 74.

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<sup>34</sup> The Council on East Asia Community (CEAC), Policy Report “The State of the Concept of East Asian Community and Japan’s Strategic Response thereto,” August, 2005, 7

<sup>35</sup> United States-Japan Security Consultative Committee Document, “Joint Statement,” May 1, 2006. <http://www.mofa.go.jp/region/n-america/us/security/scc/joint0605.html>

<sup>36</sup> Toshio Watanabe, “Higashi ajia kyodotai ha seiritsu suruka [Can East Asia community be built?]” in *Nihon no Higashi Ajia Senryaku [Japan’s Policy towards East Asian Economic Integration]*, Toyo Keizai Shinposha, 218

<sup>37</sup> Masahiro Kohara, *Higashi Ajia Kyodotai [The East Asian Community]*, Nihon Keizai Shinbunsha, 2005, 248

## 5. Diversifying Cultures and the Concept of an East Asian Community

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Discussion of a possible East Asian Community must proceed on the basis of an understanding and appreciation of the region's rich variety of cultures. What can we do to foster a sense of community among the countries of East Asia, characterized as they are by great linguistic, ethnic, and religious diversity?

### **Introduction**

#### *The Status of Culture within an East Asian Community*

It is not easy to discuss "culture" of "East Asia" area, comprising Japan, China, South Korea, and Southeast Asian countries. "East Asia" as conceived in international politics since the 1980s has been variously defined and does not necessarily correspond to an unified zone of culture. As it can be seen around the world, realms of culture do not always align neatly with political boundaries, and trying to match them up can result in friction and backlash in the political realm. The discussion of possible formation of an "East Asian Community" often proceeds without adequate consideration of culture but tends to be based on considerations in the political and economic realm in general. For the purpose of this paper, referring to East Asia as encompassing Japan, the Korean peninsula, China, and Southeast Asia (as far west as Myanmar), I will look at the diversity of cultures and value systems that is the key to forging a sense of community in this region.

### **Open to Diverse Influences**

One wonders whether any other region of the world has been as open to outside influences as East Asia, which has absorbed and assimilated incoming cultures from every direction over the millennia. The cultural center of East Asia in the narrow sense (i.e. Japan, China, and South Korea; hereafter referred to as "Northeast Asia") was undisputedly China, with its civilization formed in antiquity and with its Confucian-based traditions that spread widely throughout the region. Yet China, like all civilizations, was itself a composite of countless cultural influences from both East and West—as evident in its long history of interaction with the West via the Silk Road and also with the North and South. Historically Chinese culture has been mainly constituted by Han people and Han culture. It yielded, however, for example, to conquest from central Asia by the Mongolians, who established the Yuan dynasty, and to domination by the Qing dynasty, which brought with it a flood of cultural influences from Manchuria to the north. Thus the great civilization and the great empire of China were very much hybrid. Southeast Asia, too, has a long history of cultural contact, standing as it does between the two continental civilizations of India and China as well as absorbing Middle East culture and Muslim culture along the shipping route known as the "ocean Silk Road." The diversity of East Asian cultures is above all a product of the region's status as a crossroad between varied influences carried not only over land across Eurasia but also by sea through the Indian Ocean and the Pacific.

In more modern times, of course, came colonialism and with it the influx of Western culture. Western influences penetrated deeply even in areas like Japan, Thailand, and China that were not directly colonized by Europeans. Since the 19<sup>th</sup> century, the extent to which the region has absorbed Western culture

remains striking, the pressures to modernize notwithstanding. That receptiveness has been equally evident in the rapid assimilation of American culture that began after World War II. The countries of East Asia, both historically as well as today, can be said to share openness toward other cultures from not only within the region but far beyond its horizons.

### **Linguistic, Ethnic, and Religious Differences**

The diversity of the cultures of East Asia, as stated above, remains much more striking than their commonalities. Let me look at the mosaic of languages, peoples, and religions that covers this vast area and its implications for the creation of a sense of community there.

#### ***The World of Diverse Languages***

The diversity of East Asia is above all evident in language. Historian Miyazaki Ichisada once attempted to classify cultures based on their writing systems, analyzing the spread of right-to-left versus left-to-right writing systems mainly as it occurred in West Asia (see his *Tozai kosho shi ron* [A History of East-West Interaction], Chuo Koron Sha, 1998). He explained that left-to-right writing systems spread from Europe through Greece, Persia, and India, extending all the way to Indochina. Writing from right to left began in Egypt and traveled from Syria to Mesopotamia and Persia—both areas where a combination of right-to-left and left-to-right systems were used—and eventually across Central Asia to the Chinese border. Finally, the conquest of West Asia by Islam and the resulting adoption of right-to-left Arabic writing systems "had the effect of splitting the left-to-right group into two parts, the first stretching west of Greece and the other, east of India." Looking at the languages used today in East Asia, we find that Chinese characters are written vertically, as is Japanese, with its combination of Chinese ideograms and katakana and hiragana phonetic scripts. Korean Hangul, Thai, Burmese, and Cambodian, meanwhile, are written horizontally. Vietnamese, Malay, Indonesian, and Tagalog use the Latin alphabet and are therefore also written horizontally. All the abovementioned horizontal writing systems are read left to right, as are Chinese and Japanese when written horizontally. Japanese was once sometimes read right to left even in horizontal form, much like Arabic. Miyazaki believes that Arabic played an influential role in West Asia in spreading the practice of horizontal writing going from right to left. While none of the main (i.e., official or semi-official) languages of East Asia use Arabic orthography, we cannot overlook the fact that it is the language of Islam (e.g., the language in the Koran and the language used by their God), the religion that has more followers in this region than in anywhere else.

In short, while many of the languages of the proposed East Asian Community are written left to right, vertical writing systems take precedence in Northeast Asia and horizontal writing is the norm in Southeast Asia. Within Northeast Asia, Korea's Hangul is written horizontally, and Chinese and Japanese may be written either horizontally or vertically.

Thus unlike the languages of the European Union, which share certain basic traits, the countries of East Asia differ greatly even in terms of their writing systems alone. There is the considerable regional variation of Chinese, with its numerous dialects; although they employ a common writing system, the vernaculars spoken within China's boundaries can be as different as foreign languages. The EU has a policy of using all member state languages in discussions and providing translations in every language for all meeting records, but this would be extremely difficult, while not impossible, as far as an East Asian Community is concerned. None of the major languages of East Asia, whether Chinese (spoken by 1.3 billion people), Indonesian (roughly 200 million), Japanese (130 million), Korean (roughly 90 million in North and South Korea combined), or Vietnamese (roughly 80 million), seem suited to serve as an official language for

the entire region. Neither Chinese (Mandarin) nor any other language mentioned above qualifies as an international language, when judging by the standard of whether or not it is taught as a required foreign language in secondary and higher education in the region as a whole.

Establishing methods of communication is one of the most basic hurdles to forming an international or regional association. Unfortunately, however, none of the languages used in East Asia possesses sufficient international status to clear this hurdle. In creating an East Asian Community, the most realistic option—at least as of the present, if not the future—will probably be to adopt English as an official language, as in the case of the Association of Southeast Asian Nations (ASEAN). However, in my view, as in the case of the EU, designating all member state languages in East Asia as the official languages seems to be the best way for the future. Naturally not to be overlooked are the nearly countless minority languages being used, from the Turkic languages of the Xingiang Uygur Autonomous District in China to the numerous unwritten languages spoken across Indonesia, Malaysia, the Philippines, Thailand, and Myanmar. Whatever difficulties might come along, the community building in East Asia could not be accomplished if we are not prepared to adopt all member state languages as the official language of an East Asian Community.

### ***Ethnicity***

The diversity of ethnic groups in East Asia is as great as that of its languages. The most populous ethnic groups largely coincide with those for the languages given above. All the countries in the region are multiethnic in makeup, Japan included, but China, Indonesia, Malaysia, the Philippines, Thailand, and Myanmar have a particularly large number of ethnic groups, sometimes resulting in considerable social friction. In most cases ethnic differences mean differences in language. Every country has majority and minority groups, but often the situation is complicated by the fact that a single ethnic group may straddle national boundaries. People do not always travel across international borders voluntarily, for example for business, pleasure, or study; some are refugees from political or economic hardship, others minorities fleeing persecution.

Chinese of Han ancestry are by far the most populous ethnic group in East Asia, followed by Japanese, Koreans, Vietnamese, and Thai. Indonesia's population, although second only to China's, is a mixture of Javanese, Balinese, and numerous other ethnic groups. Only in Japan, China, the Korean peninsula, Vietnam, and Cambodia does a single ethnic group occupy over 80 percent of the population. The other countries of this region are highly multiethnic, with the possible exception of Thailand, where ethnic Thai make up just over half of the total population. Ethnic diversity is thus another dimension that distinguishes Southeast Asia from Northeast Asia.

### ***Religion***

In this region so open to and accepting of outside influences, all the major religions of the world are represented. Chinese Confucianism and Taoism, especially influential on the Korean peninsula and in Japan, Vietnam, and Singapore, can be found throughout the region thanks to the widespread settlement of ethnic Chinese. Buddhism, originally from India, is prevalent in Korea, Japan, Thailand, Myanmar, Laos, and Cambodia. Hinduism can be found not only in Malaysia, Singapore, and other areas with significant Indian populations, but wherever ethnic Indians reside. The majority of the people of Bali, located in mostly Islamic Indonesia, are Hindu. Islam is the main religion in Indonesia, Malaysia, Brunei, and several other areas in East Asia, which, as already mentioned, is home to the world's largest Islamic population. A little less than 100 million Muslims reside in China's Xingiang Uygur Autonomous District alone. Muslims live in nearly every part of East Asia, including Japan, which is host to immigrant labor from such Islamic countries

as Iran and Pakistan. Christianity, the chief religion of the Philippines, is also prevalent in such places as Hong Kong, Singapore, and South Korea, and has followings in Japan as well as almost everywhere else in the region. While perhaps not significant in terms of numbers, it still wields considerable influence due to its association with Western culture. Finally, Judaism is practiced by immigrant settlers in Shanghai and the former Manchuria, among other places.

East Asia is thus home to all five great religions of the world. Beneath the surface of these institutionalized world religions, moreover, are numerous regional folk beliefs growing out of indigenous local cultures. Folk beliefs, like China's dragon worship and fengshui geomancy, Korea's shamanism, and Thailand's *phi*<sup>1</sup> and Myanmar's *nats*<sup>2</sup> beliefs, are to be found all over East Asia. Japanese Shinto also falls into this category, the difference being that it alone is an institutionalized religion with a status equivalent to Buddhism. Shinto nevertheless stems from the same animism that is characteristic of other indigenous beliefs in the region.

As this overview of the region's languages, ethnic groups, and religions clearly shows, the overarching cultural trait of the proposed East Asian Community is its intricately intertwined diversity. Each thread exists never by itself but strictly in relation to others, giving testimony to the openness of East Asian cultures to influences from beyond their own borders. However, it is noted that the world-wide religion has the character of a state religion closely linked to the states in the region. In the case of Buddhism, there are different characteristics of Buddhism in Myanmar and Buddhism in Thailand, similarly Muslim in Indonesia differs from Muslim in Malaysia. Buddhism in Japan differs considerably from it in South Korea.

### Three Layers of Culture

While diversity is thus the defining trait of East Asia, the cultures of the region do have one thing in common: they are all hybrids. Since antiquity, efforts by societies in this region to forge their own traditions while also being exposed to countless outside influences have given birth to unique cultures, each belonging to that community alone. Even Chinese civilization is a composite of various regional cultures, as is evident not only in its language but also in the richness of its lifestyles, arts, and cuisines. The powerful influence of China did not prevent Korea and Japan from creating their own cultures. Indonesia and Malaysia, too, maintained their distinctiveness despite influences from India and, via ocean routes, from Islam; and the same can also be said for continental Southeast Asia, sandwiched between the two civilizations of China and India. Modern Western culture has obviously been yet another major influence in East Asia, while local indigenous traditions of the kind described above in the section on religion also continue to prevail. The present-day cultures of East Asia can thus be generally described as consisting of three layers: (1) indigenous local traditions, (2) traditions introduced from the great Asian civilizations, and (3) Western culture from Europe and the United States.

Societies displaying this three-layered character are to be encountered everywhere in East Asia. In Japan, for example, the Jomon culture and Shinto, among others, represent our basic and most ancient heritage. This is overlaid with our own traditions of Confucianism, Taoism, and Buddhism developed out of interaction with continental Asian civilizations, finally followed by influences from Western culture including modern science, technology, and thought. What is most remarkable about these three layers is the

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<sup>1</sup> Spirits, ghosts, phantoms, and any other kinds of presence that can be felt spiritually but not physically. Although originally a form of native animism, *phi* worship has intertwined itself with Thai Buddhism to the point of becoming utterly inseparable.

<sup>2</sup> Also *nat*, supernatural spirits and tutelary deities similar to *phi* in Thailand. There are thirty-seven recognized *nats*, including tree spirits, local deities, village guardians, and hero gods.

way they mix and mingle within present-day Japanese culture. Although quite heterogeneous elements in and of themselves, they complement rather than conflict with each other, giving shape to Japan as it is today. Far from merely absorbing all outside influences as they come, Japan has been selective about what it accepts, picking out aspects that seem meaningful and, once taking them in, turning every one of them—regardless of their different origins—into indispensable components of its hybrid culture. In Thailand, to give another example, the foundation layer consists of the indigenous culture of the kind seen in *phi* worship, which is in turn overlaid by influences from the two great Asian civilizations of India and China. Among these influences are Hinduism and Brahmanism, traces of which remain most strongly today in court ritual and folk belief; Buddhism, considered the state religion; Confucianism and Taoism, which is found mostly among ethnic Chinese but has also penetrated society as a whole, as evidenced by the surprisingly large number of Taoist deities enshrined in Buddhist temples; and various aspects of daily life culture, for example, cooking. Finally on top of all these elements comes modern Western culture.

This pattern of hybridization is to be seen everywhere throughout East Asia. The differences in the details of the process actually traced by each community account for the variations in their respective present-day cultures, giving rise to tremendous diversity and making cultures immediately identifiable as Japanese, Thai, or Korean, for example. While it is certainly possible to speak of historically traditional cultures, there seem to be no purebred ones. Every East Asian culture as it exists today is a product of each society's efforts to derive its own unique culture out of the ever-continuing processes of hybridization and cultural change. This quality is what both unites and distinguishes these cultures all at the same time.

### **Globalization and Cultural Exchange**

Rapid economic development in East Asia since the late 1980s has resulted in the rise of what may perhaps be termed an urban middle class in many of its major cities. This stratum, which in Japan first appeared in the late 1960s, has since then become the dominant social stratum in that country. It now seems, however, that a middle class composed mostly of salaried workers—what I have elsewhere called Japan's "middle class society"—is beginning to take shape to varying degrees in other East Asian societies as well. After first emerging in South Korea, Taiwan, Hong Kong, and Singapore, it has appeared in other cities such as Bangkok, Jakarta, and Kuala Lumpur since the 1990s, albeit to a somewhat lesser degree. The influence of its members on their societies has only strengthened following the economic crisis of the late 1990s. Chinese urban centers such as Shanghai and Beijing, too, are currently experiencing the rise of a similar segment of society.

The urban middle class generally tend to be university-educated professionals in various areas including business and civil service who are highly cosmopolitan and greatly concerned for the quality of life both of themselves as individuals as well as of their families. Eager for education but not particularly bound by tradition, religion, or narrow-minded nationalism, they prefer contemporary lifestyles. They give priority to rational judgments, but tend to be self-centered in their concerns. Prototypically urban in taste, they shy away from the staid or old-fashioned. Culturally speaking, they tend to have broad interests and to be keenly attuned to international trends. They are among the people most sensitive to the effects of globalization, and indeed their lifestyles and activities are largely what provide the driving force behind it.

Such structures as the Shanghai Opera House, the Esplanade concert hall and theater in Singapore, and the concert hall inside the Petronas Twin Towers in Malaysia would never have been built had it not been for this segment of society. The first full-fledged concert hall in Japan was built in the late 1980s, followed by the first real opera house in Tokyo in the late 1990s. Now, however, similar cultural facilities are springing up in many other East Asian cities, providing venues for vigorous cultural exchange among the

countries of the region. The Esplanade, for example, hosts everything from the London, NHK (Japan Broadcasting Corporation), and Singapore symphony orchestras to Indonesian gamelan players and female vocalists from Shanghai. The spread of the urban middle class has also spurred a convergence of cultural tastes throughout East Asia, fostering similar lifestyles and tastes for representational culture and giving rise to international or region-wide trends.

The "Korean Wave" (K., Hallyu; J., Hanryu) is symbolic of this rise in shared cultural interests across East Asia, as is the frequent invitation of (mostly classical) international musicians to the concert halls mentioned above. International exchange or joint productions by singers, actors, directors, producers, designers, and the like are today quite common in all areas of popular culture, including music; television, film, anime, manga, computer games, and fashion. Not only do such phenomena bear the seeds of an emerging pan-East Asian culture, but they also indicate the emergence of the kinds of creators and audiences necessary in bringing such seeds to flower. Notably, international exchange is also growing in the areas of higher education and academic research, leading to such effects as increases in the number of students studying abroad, greater interaction among researchers, and more partnerships between universities and research institutions of different countries.

The degrees to which people participate in the above stated social and cultural phenomena vary according to place, of course, and naturally not everything is proceeding in exactly the same way in all parts of eastern Asia. Nor does everything actually need to be the same; after all, regional differences are the norm even within a single country, for example between urban versus outlying areas in Japan. The urban middle class of Yangon differs vastly from that of, say, Bangkok. Yet when I traveled to Yangon in January 2004 to investigate Myanmar cultural policy, I was surprised at how much in common the tastes of university students and other youth in the city (e.g., as regards pop music, film, television dramas, anime, and manga) have with those of young people in Bangkok or Tokyo. The budding spread there of people with mindsets similar to the rest of Asia made me feel that the day might not be so far off when Yangon might become culturally quite like Tokyo, Shanghai, or Bangkok. Hanoi and Phnom Penh give one the exact same feeling. Responses to globalization vary from one country to another, and some places will always be more traditionally oriented than others; in Myanmar, for example, state policy requires citizens to wear traditional dress (called longyi), so that T-shirts and jeans are never seen even on university students. Still, there is no doubt that cultures are, in a broad sense, converging all across eastern Asia.

Indeed, such cultural mixing and globalizing as well as the widespread sharing of cultural interests made possible through information technology seem now to be inspiring the emergence of what may perhaps be termed pan-East Asian qualities in the representational cultures of Korea, China (Hong Kong), Taiwan, and Japan, among others—a phenomenon that, coupled with the emergence of a social class willing to support such trends and the rapid flow of cultural influences across borders, may have succeeded for the first time in laying down the beginnings of what could one day become the cultural foundations of an East Asian Community. Fostering these beginnings into a fully developed East Asian identity will require unceasing cultural interaction and efforts to promote deeper mutual understanding as well as cooperation on the part of potential member nations in stimulating the mutual growth of their diverse but connected cultures. With such due respect for “the cultural diversity”, we are about to lay down the first step to achieve a mutual awareness in an East Asian Community by creating common “East Asia culture” and promoting mutual understanding through cultural interaction. The further development of these actions would pave the way for East Asia to become one community in the future.

*(The preliminary updated text of the essay by Prof. AOKI Tamotsu, which originally appeared in the winter 2006 issue of the English edition of “GAIKO FORUM”.)*

## **6. East Asian Community and the United States: U.S. View --One Step Forward, Two Steps Back?**

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In the past 12 months, there has been a great deal of movement surrounding the effort to establish an East Asia community. I hasten to add, however, that “movement” does not necessarily or always mean progress. Not all the movement has been in the forward direction. Some has been sideways, some even backwards. While it would be unkind to describe the process as “one step forward, two steps back,” there certainly has not been any “great leap forward” either.

The one step forward was the convening of the inaugural East Asia Summit (EAS) in Kuala Lumpur in December 2005 and the efforts since then to develop the principles and modalities that will define the future role and mission of this new multilateral gathering. But, as continued disputes and confusion over its composition, direction, and relationship to both broader and more selective existing mechanisms reveal, East Asia community-building still has a long way to go. It is also clear to this author that the EAS will not provide the foundation of an East Asia community, but rather is more likely to serve as a broader-based endorsement or validation mechanism for a companion East Asian-only effort. In this respect, the EAS may prove to be one step backwards rather than toward the establishment of an East Asian community.

Meanwhile, it remains difficult to discuss U.S. attitudes toward East Asia regionalism or the development of an East Asian community since an East Asian community has yet to really be defined—much less credibly emerge. Generally speaking, the United States has been an active partner in many of the institution-building and/or community-building efforts that have emerged in East Asia during the post-Cold War era, including the two preeminent Asia-Pacific multilateral organizations, the Asia Pacific Economic Cooperation (APEC) “gathering of economies” which includes (at U.S. instigation) an annual “Leaders Meeting,” and the security-oriented, ministerial-level ASEAN Regional Forum (ARF).

In recent years (unlike the early 1990s), Washington has been generally supportive of—or at least not actively opposed to—even those multilateral organizations in which it was not a member, such as ASEAN Plus Three (A+3), which is comprised of the ten ASEAN countries (Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand and Vietnam) plus China, Japan, and the Republic of Korea. In fact, the Bush administration, despite its (sometimes-deserved) reputation for unilateralism elsewhere, has been particularly supportive of East Asian and broader Asia-Pacific multilateralism.

Bush administration attitudes may be changing, however. At a minimum, serious questions are now being raised regarding the nature, intent, and future direction of East Asia community-building in general and the EAS in particular, and about the motivation of some of its key proponents. As noted at this gathering last year, one lingering question, at least from an American perspective, is the extent of U.S. involvement in East Asia community-building; should Washington be included as a member, or as an observer, or not at all, in this evolving East Asia community? Arguments can be made both pro and con. How and why Washington is excluded could be as important

as whether or not it is invited to participate.

When it comes to the EAS, it is not clear if Washington even desires a seat at the table—getting President Bush to two Asian summits in any given year, especially if scheduled only a few months apart, would be no mean feat, not to mention the problem of bringing President Bush into direct contact with the leader of Myanmar, whose legitimacy Washington does not recognize. Nonetheless, the Bush administration has made it clear that it is interested in learning more about the composition of the group, the criteria for membership, and most importantly (and still largely undefined) its mission, objectives, and priorities.

To date, the Bush administration has not rejected some form of U.S. involvement in the EAS. Last year, in the run-up to the inaugural EAS, I raised a number of questions regarding the nature and intent of the EAS and the broader East Asia community-building effort. In this paper, I will revive those questions and provide answers where possible, while highlighting new and remaining questions which still preclude determination of a definitive U.S. position.

Before looking at more recent events, it is helpful to remember how we got to where we are today. As a result, I will first review Washington's evolving attitude toward multilateral cooperation and regionalism in East Asia, to ascertain what kind of ultimate response one should expect from the United States regarding regional attempts to further develop an East Asian community—with or without Washington's direct participation. I will provide *an* American perspective, not *the* American perspective. This paper represents my personal views, while merely speculating about the evolving and future views of the U.S. government, which remains generally circumspect on the subject.

In the final analysis, much will depend on who leads the East Asian community. Will ASEAN remain in the driver's seat? If so, can 10 drivers steer a steady course? If not, who will emerge? As the real economic giant in East Asia, one could argue that leadership should go to Japan. Ironically, a decade ago, when others in the region seemed prepared to accept Japan as the so-called "lead goose," Japan was hesitant to assume this role. Today, Tokyo seems more willing to take a leadership role (this remains debatable). However, "history" issues, many self-inflicted, have made it difficult for Japan to emerge from the shadow of its own past, even as it seems to be entering into the shadow of the region's emerging new giant, China. Will China be the presumptive or de facto leader of this new East Asia Community? If so, will that leadership be benign or will it be aimed—or be perceived by the U.S. as being aimed—at limiting or replacing Washington's (and Tokyo's) influence in the region

It is also important at the onset to put East Asia regionalism into context. No one seems to be promoting or anticipating a European Union-type arrangement. Attempts by Indonesia over the past few years to bind ASEAN more closely together, through the establishment of an ASEAN Community (comprised of an ASEAN Security Community, an ASEAN Economic Community, and an ASEAN Socio-Cultural Community) have shown just how difficult it is to get these nations—some of which have been closely aligned for over 30 years—to think and act as one, especially in the security arena. Developing a lowest common denominator for security cooperation among these ten diverse nations is difficult enough; imagine adding China and Japan to the mix (much less one or both Koreas). If current established multilateral community-building mechanisms, such as the ASEAN, A+3, the ARF, and APEC are any indication of the willingness of East Asian nations (regardless of how the term is defined) to seriously address issues of regional governance (and the "interference in one another's internal affairs" that true regional governance requires), one should not expect much progress soon.

Most importantly, from a U.S. perspective, will be how an East Asian community relates to the region's other multilateral organizations and initiatives—both institutionalize (like the ARF and

APEC) and ad hoc (like the Six-Party Talks and the Proliferation Security Initiative). Its relationship to the ARF and APEC in particular will be part of what Assistant Secretary of State Christopher Hill has referred to as the “Pan-Asianism vs. Pan-Pacificism” debate. Another key factor affecting Washington’s attitude will be the willingness (or lack thereof) of emerging East Asia mechanisms to adopt global norms, especially in the areas of counter-terrorism and counter-proliferation and the promotion of free and open markets. Will the new East Asia community reinforce existing multilateral efforts to accomplish these goals or dilute them? Will it help the states of the region to more effectively address growing transnational challenges . . . or provide another excuse for avoiding such efforts? These questions and some preliminary answers will be explored in this paper.

## **Background**

During the Cold War and immediate post-Cold War era, Washington’s leaders (and most other regional policy-makers) viewed the idea of institutionalized East Asia multilateral security cooperation with a great deal of apprehension and suspicion. In 1991, when then-Japanese Foreign Minister Nakayama suggested at an ASEAN Post-Ministerial Conference (PMC) gathering that a forum be established to discuss regional security issues, his remarks were not well-received. The U.S., under President George H.W. Bush, was particularly cool to such an idea. More comfortable with a one-on-one approach to security issues in Asia, U.S. officials at the time were hesitant to embrace multilateral approaches to addressing security concerns.

As the Cold War faded into history, however, there has been a decided shift in regional attitudes toward, and U.S. support for, multinational security initiatives in Asia. On the U.S. side, the first clear signal of this shift came in 1993 when then-Assistant Secretary of State for East Asian and Pacific Affairs Winston Lord identified “a commitment to enhanced multilateral security dialogue” as one of the incoming Clinton Administration's ten priority policy goals for Asia.

Of equal importance, voices were concurrently being raised within ASEAN calling for the introduction of security-related issues into PMC deliberations. One significant example occurred at the 1992 ASEAN PMC in Manila when a joint statement was issued calling for the peaceful settlement of territorial disputes involving the Spratly Islands (claimed in whole by China and Taiwan and in part by Brunei, Malaysia, the Philippines, and Vietnam). While ASEAN had been in existence since 1967, it had historically been reluctant to delve into security matters, even amongst its own members, much less with its external dialogue partners.

Regional non-governmental organizations (NGOs) were also calling for greater multilateral security dialogue both at the official and NGO level. In 1991-92, the Honolulu-based Pacific Forum CSIS joined forces with the Seoul Forum for International Affairs, the Japan Institute for International Affairs, and ASEAN ISIS—a loose coalition of Southeast Asian institutes focusing on Asian security and international studies—to promote formalized track-two (non-governmental) and official security dialogue. Their leadership led to the establishment in late 1992/1993 of the Council for Security Cooperation in the Asia Pacific (CSCAP), an NGO focused on multilateral security dialogue and regional confidence building. The CSCAP founding statement also strongly endorsed the creation of official security dialogue mechanisms.

President Clinton added the icing to the cake in July 1993 when he firmly embraced the concept of multilateral security dialogue in Asia, calling it one of the four pillars of his vision for a “new Pacific community.” This change in attitude was solidified at the 1993 ASEAN PMC meeting when the PMC dialogue partners met informally over lunch with representatives from China, Russia,

Vietnam (which was not yet a member of ASEAN), and other PMC observers, to talk about security matters. The group decided that they would reconvene the following year in the precedent-setting ASEAN Regional Forum.

President Clinton also proposed and then in the fall of 1993 served as the first host of what has now become an annual APEC Leaders' Meeting. (APEC itself dates back to 1989.) While focused on broader regional trade issues, this gathering of the region's heads of state quickly took on a political and at least quasi-security role, just by its mere existence. This was then followed by the July 1994 inaugural meeting of the ARF in Bangkok, which again provided a clear signal that attitudes regarding multilateral security dialogue were changing, both in the United States and throughout Asia.

While instituted during the Clinton era, both the ARF and the APEC Leaders Meeting have thus far enjoyed strong support from the current U.S. administration as well, witness President George W. Bush's willingness to attend the October 2001 Shanghai APEC meeting in the immediate wake of September 11<sup>th</sup> and the presence of Secretary of State Colin Powell at all four ARF meetings held during his tenure in office (something neither of his predecessors could claim).

While Secretary of State Condoleezza Rice (deservedly) received widespread criticism for missing her first ARF meeting in July 2005—she was ably represented by her Asia-oriented deputy, Robert Zoellick—Washington has reaffirmed its commitment to the ARF several times since then and has sent strong assurances that Dr. Rice will be at the 2006 meeting in Malaysia.

The Bush administration's early support for East Asian multilateralism was reinforced in the White House's September 2002 *National Security Strategy for the United States of America (NSS)* which expressed the conviction that "multilateral institutions can multiply the strength of freedom-loving nations" and further stated that the U.S. would build upon the stability provided by institutions such as ASEAN and APEC "to develop a mix of regional and bilateral strategies to manage change in this dynamic region."

This was reinforced in the 2006 *NSS*. Consistent with its theme of promoting freedom and democracy, it noted that existing institutions like the ARF and APEC can play a "vital role" when it comes to "the spread of freedom, prosperity, and regional security." It also noted that "new arrangements, such as the U.S.-ASEAN Enhanced Partnership, or others that are focused on problem-solving and action, like the Six-Party Talks and the PSI [Proliferation Security Initiative], can likewise bring together Asian nations to address common challenges."

In short, the Bush administration has renewed and reinvigorated U.S. interest in the ARF and APEC and, against some initial regional resistance and criticism, insisted on a multilateral approach, under the Six-Party Talks, for dealing with the North Korean nuclear problem. On a somewhat more contentious note, it has also placed a great deal of importance on "ad hoc multilateralism"—the PSI, for example, serves as a primary vehicle in the U.S.-led global effort to counter the proliferation of weapons of mass destruction. How such "coalitions of the willing" will interact with standing multilateral mechanisms, or for that matter with Washington's traditional bilateral alliances, has yet to be fully determined, however.

### **Pro-Multilateralism, with Caveats**

As a general rule, Washington has historically viewed Asia Pacific multilateral organizations as useful vehicles both for promoting greater political and economic cooperation and for enhancing regional security. This support for multilateral institutions—in the Asia Pacific and globally—has one important caveat, however: No U.S. administration, be it Republican or Democrat, is likely to allow

such institutions to be seen as substitutes for or as threats to U.S. bilateral alliances and other security arrangements.

This was clearly spelled out in the 2006 *NSS*: “Asian nations that share our values can join us in partnership to strengthen new democracies and promote democratic reforms throughout the region. This institutional framework, however, must be built upon a foundation of sound bilateral relations with key states in the region.” Like the Clinton administration before it, the Bush administration does not see bilateral and multilateral efforts as being in tension; rather, they complement one another. As a general rule, East Asian multilateral organizations are seen as useful tools in pursuing U.S. national security objectives.

During its first term in office, the George W. Bush administration was also cautiously supportive of multilateral organizations, such as ASEAN Plus Three and the Shanghai Cooperation Organization (SCO), which do not include the U.S. In its second term, however, the Bush administration is starting to cast a more watchful eye, especially on those organizations established and/or dominated by China, to ensure that these do not represent efforts to diminish Washington’s (or Tokyo’s) involvement or interests in the region.

This has been especially true since July 2005, when the Beijing (and Moscow)-driven SCO (which also involves four Central Asian states: Kazakhstan, Kyrgyzstan, Tajikistan, and Uzbekistan) called for the U.S. to set a date for the withdrawal of its forces from Central Asia during a summit meeting in the Kazakhstan capital of Astana. The SCO proclamation called on the U.S. and its coalition partners to “decide on the deadline for the use of the temporary infrastructure and for their military contingents’ presence” in Kyrgyzstan and Uzbekistan—at the time, the U.S. had roughly 1,000 troops each at airfields in Karshi-Khanabad in Uzbekistan and Manas in Kyrgyzstan—“as the active military phase in the anti-terror operation in Afghanistan is nearing completion.”

By the end of that month, it became obvious that one of the hosts—Uzbekistan, which had come under increasing criticism from the U.S. and the international community in general for its harsh repression of protestors in Andijan in May—was not going to wait for the U.S. to set its own deadline; on July 29, Uzbekistan gave Washington 180 days to vacate Karshi-Khanabad. While this no doubt reflects Uzbek President Islam Karimov displeasure over Washington’s criticism of his dismal human rights record, it is doubtful it could have occurred without Moscow and Beijing’s consent, if not active encouragement and support. As a result, this action has raised serious questions about Beijing’s (and Moscow’s) motives, and resulted in a more watchful eye being cast on exclusionary East Asia multilateralism.

While the U.S. is still not attempting to actively block or interfere with East Asia regionalism efforts like the A+3 and SCO that exclude the U.S., it is closely monitoring their future direction and carefully examining the motives of those who seek to guide them. Meanwhile, the Bush administration continues to state its clear preference for “inclusive” Asia-Pacific regional efforts that include Washington, despite some of the inherent perceived weaknesses.

A brief examination of Washington’s involvement in and attitude toward the region’s two premier broader Asia-Pacific community-building organizations—the ARF and APEC—may lend some insight into its view of East Asia regionalism in general.

### **The ARF: “Very, Very Useful” but Limited**

The 25-member ARF brings together foreign ministers from the ten ASEAN states plus Australia, Canada, China, the European Union, India, Japan, Mongolia, Papua New Guinea, Russia,

South Korea, North Korea, New Zealand, and the United States, plus Pakistan (since 2004) and most recently (2005) Timor-Leste, for annual security-oriented discussions. It received broad support during the first four years of the George W. Bush administration, being described by then-Secretary of State Powell as “very, very useful” after his first ARF meeting.

As noted earlier, Secretary of State Condoleezza Rice missed her first opportunity to participate in the ARF when “scheduling conflicts” caused her to miss the July 2005 ministerial in Vientiane, Laos; an omission that openly raised questions about Washington’s continued commitment to East Asia regionalism and was deemed “unfortunate” by ASEAN leaders. However, the presence of her deputy, Robert Zoellick (a highly respected old Asia hand) helped to assuage these concerns. At a 10+1 side meeting with ASEAN ministers, Zoellick helped to initiate a US-ASEAN Enhanced Partnership proposal to deepen U.S. cooperation with the ten Southeast Asian nations on a broad range of issues.

Various ARF study groups (called Inter-sessional Support Groups or ISGs) have provided a vehicle for the U.S. to move the multilateral process along in areas important to Washington, such as preventive diplomacy, enhanced confidence building, counter-proliferation, and maritime (including search and rescue) cooperation; all of which help promote greater transparency and military-to-military cooperation. Most importantly, since Sept. 11, 2001, the ARF has helped focus regional attention on, and has served as an important vehicle for practical cooperating in, fighting terrorism.

At the ARF meeting in Jakarta in July 2004, the assembled ARF Ministers repeated annual pledges to fight terrorism and the spread of weapons of mass destruction through ARF Statements on “Strengthening Transport Security Against International Terrorism” and a “Statement on Non-Proliferation.” They also confirmed their intentions to further institutionalize the ARF process through the establishment of “an ARF Unit” within the ASEAN Secretariat to serve as a *de facto* ARF Secretariat, to assist “in carrying out the mandates outlined in the paper on the Enhanced Role of the ARF Chair” and to support the Experts and Eminent Persons Group.

Annual counter-terrorism pledges were repeated at the 2005 ARF Meeting in Vientiane, Laos in July 2005, with China and Brunei agreeing to host an Inter-sessional Meeting on Counter-Terrorism and Transnational Crime. The big news coming out of Vientiane was the announcement that Myanmar would skip its turn, after Malaysia, to chair ASEAN (and hence the ARF) in mid-2006, thus avoiding a confrontation between ASEAN and Washington (among others), who had pledged to send only low-level representatives to any ARF meeting hosted by Myanmar.

Generally speaking, the ARF seems well-suited to serve as the consolidating and validating instrument behind many security initiatives proposed by governments and at non-official gatherings, and has become a useful vehicle in the war on terrorism. But, from a U.S. perspective, its contribution to the regional security order remains somewhat constrained. For example, Taiwan has not been permitted to participate and the PRC has insisted that “internal Chinese affairs” not be on the agenda, effectively blocking ARF discussion of cross-Strait tensions despite their obvious broad regional implications. The Chinese have even been reluctant to address conflicting claims in the South China Sea at the ARF, insisting instead on separate talks with ASEAN or with the other claimants on an individual basis.

Few expect the ARF to solve the region’s problems or even to move rapidly or pro-actively to undertake that mission. The agreement to “move at a pace comfortable to all participants” was aimed at tempering the desire of more Western-oriented members for immediate results in favor of the

"evolutionary" approach preferred by the ASEAN states, which all too often seems to see the process as being as (or more) important as its eventual substantive products. The Asian preference for "noninterference in internal affairs" also has traditionally placed some important topics essentially off limits, although this may be changing (witness ASEAN's increased willingness to comment on Myanmar's domestic politics). Nonetheless, it seems safe to assume that the evolution of the ARF from a confidence building measures "talk shop" to a true preventive diplomacy mechanism (as called for in its 1995 Concept Paper) will be a long and difficult one.

### **APEC: Cautiously Testing the Security Waters**

APEC is first and foremost a "gathering of regional economies"—it is not referred to as a gathering of states or governments due to the presence in its ranks of Hong Kong and Taiwan. It started out as an informal dialogue group, growing from an original 12 members (Australia, Brunei, Canada, Indonesia, Japan, the Republic of Korea, Malaysia, New Zealand, the Philippines, Singapore, Thailand, and the United States) in 1989 to 15 in 1991 (with the addition of China., Hong Kong, and "Chinese Taipei") to its current strength of 21, with the addition of Mexico and Papua New Guinea (1993), Chile (1994), Peru, Russia, and Vietnam (1997). Institutionalization began in February 1993, when the APEC Secretariat was established in Singapore.

While primarily aimed at managing the effects of growing economic interdependence, APEC has had an important political and security role as well, especially since the 1993 Seattle meeting when President Clinton invited the APEC heads of state and government to the first of what have now become regular annual Leaders' Meetings designed to elevate the importance of this economic gathering. The Leaders' Meetings have become an important vehicle for fostering political relations in addition to raising the level of economic dialogue and putting pressure on the region's leaders (and especially the host state) to move the process forward.

### **APEC's Evolving Political/Security Role**

The political and even strategic significance of the Leaders' Meetings was first underscored in Auckland in 1999, a gathering that was significant more for what happened outside the APEC venue than inside the meeting. Security issues dominated the side discussions and the talk in the corridors. Not the least of these was the growing (and well-founded) concern over the deteriorating security situation in East Timor. The Auckland meeting was fortuitous in that it provided an opportunity for regional leaders, including President Clinton and Australian Prime Minister John Howard, to work out arrangements for the Australian-led multinational peacekeeping mission (INTERFET) that was subsequently sent to East Timor. Obtaining on-the-spot Chinese approval of this effort, made possible by Indonesia's reluctant acceptance of the intervention, helped assure UN Security Council authorization of the subsequent UN operation, the United Nations Transitional Authority in East Timor (UNTAET). (It should be noted that neither ASEAN nor the ARF were major players in the East Timor crisis, demonstrating their limited utility as crisis response mechanisms.) This remains the case today, with Malaysia alone among ASEAN providing military assistance to Timor-Leste in response to recent cries for help.

In similar fashion, APEC 2001 provided an important vehicle for President Bush to explain Washington's war on terrorism to his Asian colleagues and to garner their support. In addition to the usual annual APEC Leaders' Declaration, the assembled leaders also issued an APEC Leaders' Statement on Counter-Terrorism—the first political document to be issued in APEC's 13-year

history—which unequivocally condemned the September 11 attack and deemed it “imperative to strengthen international cooperation at all levels in combating terrorism in a comprehensive manner.” This was considered a real victory for President Bush and no doubt helped to increase APEC’s (or at least the Leaders Meeting’s) relevance in his eyes.

The APEC Shanghai meeting also provided President Bush with his first opportunity to meet directly with Chinese President Jiang Zemin, which helped to end the downward slide in Sino-U.S. relations underway since Bush’s inauguration (and especially after the collision between a U.S. reconnaissance plane and a Chinese jet fighter over the South China Sea in April 2001). The two leaders were able to put the relationship back on track, aided by China’s willingness to cooperate in the battle against terrorism.

Security matters continue to be discussed at the Leaders Meeting, not to mention at the numerous side summits that normally accompany this gathering. For example, at the October 2003 APEC Leaders Meeting in Bangkok, the final communique referred to cooperation on combating proliferation of weapons of mass destruction (WMD), while President Bush used the occasion, and his side meetings with the leaders of South Korea, Japan, and China, to call on North Korea to abandon its nuclear weapons aspirations, while repeating his offer to provide Pyongyang with written assurances that the U.S. does not intend to attack North Korea. Similar efforts took place at the 2004 APEC Leaders Meeting in Santiago, Chile and at the November 2005 APEC meeting in Busan, Korea.

At the Busan Leader’s Meeting, the major focus was on a strong statement in support of the critical World Trade Organization (WTO) Doha Development Agenda round slated to take place the following month (with little success) in Hong Kong. In addition to other agreements on energy cooperation, on a roadmap to assess progress on the Bogor Goals of trade liberalization, and on several anti-terrorism measures, APEC leaders also agreed to establish the “APEC Initiative on Preparing for and Mitigating an Influenza Pandemic.” (After the tsunami disaster in late 2004, government leaders became more alert and responsive to the need for a collective approach to prepare for such cross-border threats.)

President Bush met jointly with the six ASEAN members of APEC along the sidelines of the 2005 APEC Leaders Meeting, in what constituted his first-ever U.S.-ASEAN Summit and which resulted in a desire, by all concerned, for continued meetings. Discussions are now underway to make this a regular event. The setting is particularly attractive to Washington since Myanmar is not a member of APEC.

As long as APEC provides a useful venue not only for the promotion of free trade but also for fighting the war on terrorism, we can expect that Washington will continue to be an active player. However, as with the ARF, it will remain more suited to talking about security problems than to actually helping to implement solutions. In addition to the usual drawbacks associated with East Asian multilateralism (as discussed below), APEC has the added “problem” of including Taiwan. Rather than using this venue as a vehicle for incorporating Taiwanese views and concerns into the regional security debate in a “non-governmental” setting, Beijing has tried to block any substantive security-oriented activities and to further isolate Taiwan from the dialogue process.

### **Multilateral Pluses and Minuses**

In short, American policymakers generally believe that Asia-Pacific multilateral organizations such as the ARF and APEC are useful vehicles both for promoting greater political and economic cooperation and for enhancing regional security. While such organizations hold many promises for

Asia, it is important to understand their limits, as well as the opportunities they present. A comprehensive security arrangement or NATO-type alliance aimed at containing or responding to a specified threat simply does not apply to a post-Cold War Asia. Rather, East Asia multilateral security mechanisms should be viewed more as confidence building measures aimed at avoiding or dampening the possibilities of (rather than reacting to) crises or aggression. Peacekeeping and disaster relief operations and non-traditional security issues (such as refugee problems, maritime safety, pollution, and other environmental and safety issues) also seemed well-suited to a multilateral approach. In many instances, the process is as important as the product.

Efforts that build upon and seek to complement, and not to replace, existing bilateral and ad hoc relationships that already exist in Asia are of particular value from a U.S. perspective. Any effort that is perceived as undermining U.S. bilateral dealings, and especially those that seek to diminish or replace America's key bilateral security alliances, are sure to be rejected by Washington both today and by any future administration.

More generally speaking, Asian multilateral security mechanisms can serve as important vehicles for promoting long term peace and stability. They provide a framework for continued direct U.S. involvement in regional security matters. They offer a means for Japan, China, and Russia, among others, to become more actively involved in regional security affairs in a manner that is non-threatening to their neighbors. They also provide a forum for exposing North Korea to regional realities while facilitating bilateral dialogue between the North and South Korea, Japan, and the U.S., respectively. They also provide a mechanism for other regional actors to be heard, while contributing to a sense of regional identity and a spirit of cooperation and confidence building. Since Sept. 11, 2001, they have also become increasingly relevant for coordinating regional views and efforts in the war on terrorism.

Nonetheless, their utility remains limited, especially in the security arena, for two primary reasons. First, while steps have been taken since the 9-11 terrorist attacks to put some operational substance behind cooperative efforts, these organizations still largely remain dialogue mechanisms which talk about – rather than respond to or deal effectively with—emerging security challenges. And second, Taiwan has been systematically excluded from many of these mechanisms and one of the region's greatest security challenges—cross-Strait relations—has been purposefully kept off the security dialogue agenda at Beijing's insistence. As long as these characteristics prevail, the prospects and promises of multilateral security cooperation in the Asia-Pacific region, at least from a U.S. perspective, will necessarily be limited.

### **Ad Hoc Multilateralism: The PSI and Six-Party Talks**

If Washington has only limited confidence in institutionalized multilateral mechanisms (like the ARF, APEC, and the United Nations), it is developing a clear preference for ad hoc or tailored multilateralism aimed at a specific task or objective and comprised of a “coalition of the willing.” The multinational force assembled for the war in Iraq provides one example, as does the aforementioned Proliferation Security Initiative.

### **Proliferation Security Initiative**

The PSI was first laid out in a speech by President Bush in May 2003 and formalized at a 11-nation meeting (involving Australia, France, Germany, Italy, Japan, the Netherlands, Poland, Portugal, Spain, the UK, and the U.S.) in Madrid a month later. It is “a global initiative with global

reach,” under which coalition members have agreed “to move quickly on direct, practical measures to impede the trafficking in weapons of mass destruction (WMD), missiles, and related items.” As such, it is clearly “task-oriented.” It represents cooperation for a specific, clearly-defined purpose, as opposed to dialogue for dialogue’s sake or in support of more generic objectives. In Sept. 2003, in Paris, the 11 core participants agreed on a Statement of Interdiction Principles “to establish a more coordinated and effective basis through which to impede and stop [WMD] shipments . . . consistent with national legal authorities and relevant international law and frameworks, including the UN Security Council.” Over 70 nations have expressed support for these principles.

Other major Asia-Pacific participants beyond the initial PSI core group include Canada, the Philippines, Russia, and Singapore. Others, like China and South Korea, claim they support the PSI’s objectives but have refrained from directly participating, in part due to North Korean objections. PSI participants have conducted numerous air, ground, and (mostly) sea interdiction exercises to develop and demonstrate its capability to prevent illicit trafficking in nuclear weapons and fissile material. In October 2004, Japan for the first time hosted a PSI interdiction exercise in Tokyo Bay, involving nine naval and coast guard ships from Australia, France, Japan, and the U.S., providing yet another example just how deeply involved Tokyo has become in bilateral and multilateral security cooperation. The most recent Asia-Pacific exercise was hosted by Australia.

### **Six-Party Talks**

The best example of task-oriented ad hoc multilateral cooperation in Northeast Asia is the Six-Party Talks, established by Washington to deal with the specific issue of denuclearization of the Korean Peninsula. The talks were also intended, and served, to multilateralize what many initially viewed as a bilateral U.S.-DPRK problem.

The creation of the six-party process, in this author’s opinion, may represent one of the Bush administration’s finest diplomatic hours. [Please note that I am addressing here the *creation* of the multilateral process, not its results to date.] This initiative draws from the lessons learned during the first North Korea nuclear crisis, where—despite close coordination and consultation—Washington was widely perceived as unilaterally cutting a deal with Pyongyang before sticking Seoul and Tokyo with the bill. While Pyongyang argued for bilateral consultations (and a separate U.S.-DPRK non-aggression pact), Washington rightfully insisted this time that participation by Seoul and Tokyo was “essential.” It also acknowledges the important role that China, and to a lesser extent Russia, must play if multilateral security guarantees are to be part of the final solution (as most would agree they are). Finally, the Bush administration recognized and tried to work around Pyongyang’s strategy of trying to play all sides against one another by presenting different, conflicting messages depending on the audience.

All this is not to argue that the crisis could not have been handled better; it is to say that the multilateral approach represents the most logical avenue toward crafting a long-term solution that achieves not only Washington’s immediate goal of stopping nuclear proliferation but also addresses the needs and concerns of North Korea’s immediate neighbors. The concept calls for working level discussions as well as plenary sessions, in order to dig more deeply into the problems associated with the nuclear standoff and broader peninsula security issues and concerns. It also facilitates bilateral discussions within the six-party framework, thus providing political cover for direct contact between Washington and Pyongyang.

All of this presumes a resumption of the Talks and the eventual willingness of the DPRK to

honor its commitment to bring about “the verifiable denuclearization of the Korean Peninsula in a peaceful manner,” as outlined in the Six-Party Talks Sept. 19, 2005 Joint Statement, the first mutually agreed product to result from two years of sporadic meetings in the six-party framework. The Joint Statement represented the first real sign of tangible progress in identifying common principles and objectives. It may yet provide a basis for future progress, if or when North Korea makes the “strategic decision” to abandon its nuclear weapons programs and return to the negotiating table. Unfortunately, events since that date suggest that this decision has not yet been made by Pyongyang.

The creation of the Six-Party Talks mechanism provides a framework for broader Northeast Asia multilateral cooperation in the future. If the Talks eventually succeed, most parties agree that a more formalized mechanism must evolve in order to implement the agreement, provide necessary security assurances, and monitor compliance, as well as facilitate whatever aid packages are associated with the final accord. If the Talks fail, some would argue that there will be an even greater need for some form of institutionalized cooperation in order to manage the danger posed by a presumed (and self-confessed) nuclear weapons-equipped North Korea, if the other parties are prepared for this level of cooperation. If and how the six-party mechanism transitions into a more institutionalized Northeast Asia forum will help determine the degree of future security cooperation in this East Asia subregion and Washington’s involvement in it.

### **East Asia Summitry: Much Ado About Something?**

While Washington focused on ad hoc initiatives and Asia-Pacific regionalism, the states of East Asia have continued their community-building efforts. As noted earlier, in December 2005, Malaysia convened the first East Asia Summit. It should be noted that the EAS was not the only summit taking place in Kuala Lumpur at that time. ASEAN leaders also met amongst themselves, with their Plus Three partners, and in individual ASEAN Plus One meetings with their Australian, New Zealand, and Indian counterparts. This was the second time that Canberra and Wellington and the third time that New Delhi participated in this conclave. Russian President Vladimir Putin also appeared on the ASEAN summit scene for the first time, conducting his first A+1 dialogue. He was also invited to meet with, but not to officially join, the other 16 assembled leaders at the first annual so-called A+3+3 East Asia Summit.

### **Whither the EAS?**

Was the inaugural East Asia Summit (EAS) “much ado about nothing,” as many critics are already claiming, or “a historic event whose future impact is likely to be as significant as the first [1976] ASEAN summit,” as Barry Desker, head of Singapore’s influential Institute of Defence and Strategic Studies, argues? [PacNet 55B, Dec. 23, 2006, “Why the East Asian Summit Matters”] The answer is: it’s too soon to say.

While it remains unclear just what the EAS will eventually become, an analysis of the first meeting makes it fairly clear what it will not be: it will not form the base of the much-heralded but still dormant East Asia community. That role appears destined, in this author’s opinion, to remain with the more exclusive ASEAN Plus Three gathering. It is also highly doubtful that it will, or wants to, pose a threat to U.S. interests.

The EAS host, Malaysian Prime Minister Abdullah Badawi, made it abundantly clear that the ten ASEAN countries and their Plus Three partners constituted the core, noting that “You are talking about a community of East Asians; I don’t know how the Australians could regard themselves as East

Asians, or the New Zealanders for that matter.” “We are not talking about members of the community,” Badawi continued, even though Australia, New Zealand, and “our immediate neighbor” India have “common interests in what is happening in the region.” The architects of East Asia community-building, he clearly inferred, would all be Asians, with the A+3 (vice EAS) participants providing the base. While his comments indicated that India might one day be able to slip its nose into the tent, Australia and New Zealand clearly would not. A+3 would drive the train (with ASEAN hoping to remain the conductor). The EAS would provide a vehicle for outsiders to endorse the community-building effort; it “could play a significant role,” but would not be an integral part of (much less drive) the process.

For his part, Australian Prime Minister John Howard, while noting that the EAS had “exceeded my expectations,” argued that APEC, rather than the EAS or A+3, should remain “the premier body.” APEC, he noted, has the “great advantage” of including the United States. We would note that it also includes Taiwan (a.k.a., Chinese Taipei)—another “great advantage”—but excludes several of the lesser developed ASEAN states, including Myanmar (which from Washington’s perspective may be yet another plus).

The EAS Chairman’s Statement underscored, twice, that ASEAN will be the “driving force” behind East Asian community-building. The KL Declaration on the Summit declares that future meetings “will be hosted and chaired by an ASEAN Member Country . . . and be held back-to-back with the annual ASEAN Summit.” Beijing had suggested that it host the second round but ASEAN remains as concerned about sharing driving privileges with its other community members as it does allowing outsiders a greater say in the community-building process.

The Chairman’s Statement and KL Declaration both acknowledge that building an East Asia Community is “a long term goal.” First priority will go toward building “a strong ASEAN Community which will serve as a solid foundation for our common peace and prosperity.” This should make Indonesia happy: Jakarta, which had previously put forth its own proposals for building an ASEAN Community, had believed that pushing for the EAS was premature. Prime Minister Badawi had been the primary proponent of the EAS, apparently catching Indonesian President Susilo Bambang Yudhoyono (among others) by surprise when he pushed for the EAS at last year’s summit in Vientiane. That was before Australia and New Zealand were added to the mix, which clearly curbed Badawi’s enthusiasm.

### **Addressing Washington’s Concerns**

At present, there is little cause for Washington to be concerned about the EAS. Participants are quick to point out that the United States is welcome to join (even if this is a bit disingenuous, since it realized Washington’s stance on the TAC when it made signing this treaty a precondition for membership). It is not clear that Washington even desired a seat at the EAS table—getting President Bush to two Asian summits in four weeks would have been no mean feat. Nonetheless, Washington continues to watch the EAS closely to see if certain members attempt to move this embryonic organization in a direction that runs contrary to U.S. interests.

In an apparent attempt to address one of Washington’s potential concerns, the KL Declaration noted that the EAS would be “an open, inclusive, transparent, and outward-looking forum in which we strive to strengthen global norms and universally recognized values.” Washington’s membership would still require it to accede to the ASEAN Treaty of Amity and Cooperation (TAC), something the Bush administration (like its predecessors) has been reluctant to do. Observer status appears possible,

however (and is more likely to be sought by Washington).

Chinese Premier Wen Jiabao seemed to be opening the door for this when he noted that the EAS should “welcome the participation of Russia” and “strengthen contact with the United States, the European Union, and other countries.” Wen stressed that the EAS would not be “closed, exclusive, or directed against any particular party.” (Secretary Zoellick had warned Beijing that it should not use its participation in multilateral organizations like the EAS to “maneuver toward a predominance of power” or otherwise be seen as deliberately trying to undercut Washington’s influence or interests. Beijing, among others, clearly heard this message.)

Still undefined is how the EAS (or the A+3, for that matter) will interact with broader regional organizations such as APEC or the ARF. Hopefully, this will be one of the modalities to be addressed by EAS participants when they next convene in December 2006 in Cebu, Philippines. As noted at the onset, how the EAS relates to the region’s other multilateral organizations and initiatives—both institutionalized (like the ARF and APEC) and ad hoc (like the Six-Party Talks and the Proliferation Security Initiative)—will also be a key factor affecting Washington’s attitude, as will its adoption of global norms, especially in the areas of counter-terrorism and counter-proliferation. Will the EAS (or A+3, for that matter) reinforce or dilute these efforts? Will it help regional states more effectively address growing transnational challenges . . . or provide another excuse for avoiding such efforts?

The answers to these questions will help determine Washington’s attitude toward the EAS and any subsequent East Asian Community. To the extent this new grouping signals its willingness to coexist with Washington, and is not seen as threatening or attempting to undermine Washington’s bilateral alliances, its own central role in East Asian security affairs, or the broader Asia-Pacific regional institutions in which it participates, there is little reason to expect objections from Washington or a serious effort to discourage or derail this or any other regional community-building efforts.

### **TAC: Why Not Join?**

For its part, Washington should begin exploring the possibility of seeking observer status in the EAS. It should also be asking itself why it continues to resist acceding to the TAC. The oft-stated contention that this would somehow undercut America’s Asian alliances appears unfounded: two of Washington’s Asian allies—Thailand and the Philippines—are charter members of ASEAN, while the other three—Australia, Japan, and the Republic of Korea—have now acceded to the TAC without any perceptible impact on Washington’s network of bilateral alliances.

As a member of the ARF, Washington has already endorsed the purpose and principles of the TAC “as a code of conduct governing relations between states and a unique diplomatic instrument for regional confidence-building, preventive diplomacy, and political and security cooperation.” Perhaps it’s time to take the next step, in order to demonstrate its commitment to regional prosperity and stability and to underscore its support for East Asia community-building.

### **Is Community-building Possible?**

While much attention has been paid to the Bush administration’s reaction to East Asia community-building, the biggest threat to this effort comes not from Washington but from within the “community.” The sad truth is, with or without Washington’s acquiescence, East Asia community-building is not going to be easy, given rising nationalism in Japan, China, South Korea,

and elsewhere. Even within ASEAN, there are clear differences of opinion regarding the focus and intent of the EAS, especially between Indonesia and Malaysia. Meanwhile, unless and until Tokyo, Beijing, and Seoul can more effectively channel or control their respective nationalist tendencies, it is difficult to image a true East Asian community taking shape.

The primary catalyst for today's tensions has been Japanese Prime Minister Koizumi Junichiro's continued visits to the Yasukuni Shrine—he made his 2005 visit on Oct. 17 and is expected to go again this year before he relinquishes the premiership (perhaps on August 15)—along with lingering disputes over textbook renditions of history. Japanese textbooks have come under the most scrutiny, given the approval of one controversial textbook series in particular (which has been adopted by less than one percent of Japan's public schools), but textbooks in South Korea and especially China would also fail most objectivity tests (and we won't even try to add North Korean textbooks to this mix).

Prime Minister Koizumi argues that he is merely honoring his campaign pledge to continue paying tribute to Japan's war dead—there are over 2 ½ million souls interred at Yasukuni, unfortunately including 14 World War Two “Class A” criminals, the source of the controversy. But, Mr. Koizumi has also sworn to preserve, protect, and promote Japanese national security interests, and his continued annual visits to the Shrine are making this increasingly impossible to do, at least when it comes to promoting harmony in the immediate neighborhood, much less attempting to create a sense of East Asia community.

Meanwhile, the failure of the U.S. to speak out publicly on this issue, combined with the (correct) impression that the U.S. stands firmly behind Mr. Koizumi and his quest for acceptance of a greater political and security role in East Asia, has translated into increased ill will against Washington, especially from its other key East Asia ally, South Korea. President Bush was questioned repeatedly during his November 2005 visit to Japan, Korea, and China about his reaction to the “antagonizing” Yasukuni visits. While he reportedly did discuss the issue with Koizumi in private, in public, Bush repeatedly ducked the question, responding instead that “I believe a useful role for me, as someone who is friendly with the three leaders involved, is to remind people that it is best to put the past behind and move forward in the future.” Unfortunately the high profile visits make putting the past behind impossible. [For more on this topic, see PacNet #53, Dec. 6, 2005, “Yasukuni Shrine: Time to Make a Deal.”]

### **Evolving U.S. Attitudes: Pan-Asianism vs. Pan-Pacificism**

Until recently, the U.S. has been circumspect regarding the EAS and East Asia community-building in general, stating that it reserves judgment on the EAS until its mission and objectives become clear and that, in principle, it supports more “inclusive” approaches. However, during a recent visit to Southeast Asia, Assistant Secretary of State for East Asian and Pacific Affairs Christopher Hill noted that U.S. “engagement with Southeast Asia continues to broaden and deepen. The dynamism of the region means that our relationship is in a constant state of evolution, which has given rise to renewed debate and discussion about regional fora, and whether they should be inclusive or exclusive. Correspondingly, the concept of pan-Asianism vs. pan-Pacificism has also re-emerged.”

The U.S. has not objection to East Asia regionalism *per se*, Hill argued, noting that “it is entirely understandable that Asia is looking to strengthen its own regional institutions, just as other regional groupings in other parts of the world have done the same. This drive is a reflection of the remarkable and still growing pattern of intra-Asian economic and financial integration, and is not

surprising -- and we welcome it.”

Hill then repeated concerns about the proliferation of multilateral initiatives and the danger of “meeting fatigue”: “But we need to think hard and clearly about the question of how we can integrate pan-Asian and trans-Pacific fora. We have heard much debate about the East Asian Summit. Before coming to any conclusions, we need to look at the whole landscape—and indeed the seascape—of proliferating regional for a—ASEAN+3, APEC, ARF, and the EAS—to determine how the pieces can fit better together. The goal should be to achieve synergy and avoid redundancy and duplication.”

Hill also reaffirmed Washington’s concern about how the EAS would relate to broader-based multilateral efforts involving the U.S.: “With respect to the East Asia Summit, the U.S. continues to watch with interest how this forum will develop. As I mentioned earlier, APEC and the ARF are vital components of our relationship with Asia and Southeast Asia. We want to continue to work with you to ensure we don't dilute the effectiveness of these institutions and the important cooperation they foster. The United States is and will remain deeply involved in the transformation of Southeast Asia.”

### **East Asia Community-Building: Unanswered Questions**

One objective of this paper is to stimulate questions for others to answer, in order to better determine if Washington will see this phenomenon as supportive of its national security interests or designed to threaten or inhibit them. Allow me to end this paper, therefore, with a laundry list of questions (with limited commentary). Many are left over from last year’s CEAC dialogue.

- What are the objectives of Indonesia’s ASEAN Security Community (ASC) proposal and what are the prospects of ASEAN successfully pursuing this effort? Will the ASC help set a more positive security agenda for the ARF or for the emerging East Asia community? My guess is that Washington would welcome a more pro-active ASEAN that put more emphasis on security cooperation and joint approaches to security challenges. The ASC emphasis on promoting democracy and individual rights, if seriously supported and pursued, would also be in keeping with Washington’s regional and global objectives. Merely paying lip service to these objectives, on the other hand, will reconfirm negative opinions about ASEAN’s seriousness and long-term direction.

- Is Indonesia prepared to lead ASEAN in developing an ASC and in setting the agenda for the EAS? Are the other ASEAN members (and especially Malaysia) prepared to follow? Will ASEAN remain in the A+3 driver’s seat for the ASF, A+3, and emerging EAS? If not, who will lead, and in what direction? Can/will Japan step forward and exercise leadership behind the scenes and act in concert with other friends of Washington (like Singapore and Australia) to ensure that the EAS does not evolve in a manner that runs contrary to U.S. interests?

- Is the East Asia Summit the primary vehicle for building and sustaining the East Asia community? Are the two synonymous? I have already argued that they are not, but the distinction has yet to be made by the EAS itself. The relationship needs to be better defined, since there are many competing views of what constitutes East Asia and what vehicles will best create this sense of community. Since the various multilateral initiatives provide a mind-boggling array of combinations (one even includes Persian Gulf countries), it is getting more and more difficult even to define East Asia, much less to determine which effort or efforts are helping to establish the desired sense of community. India’s future role is of particular interest here.

- Who gets to come to the EAS, in what capacity, and by what criteria? The EAS was initially envisioned as part of the A+3 process but appears destined to go beyond these 13 states. Why? How do the A+3 and EAS differ? What is the EAS mission statement and objectives? (To date, more time has been spent debating about who should join than determining what should be discussed.)

- The creation of the EAS, as called for in the A+3 Vision 2020 Plan, was seen by some as an effort by the larger East Asia powers, like China, Japan, and/or even the ROK, to try to gain increased control in shaping the agenda, a role up to now largely played by ASEAN. Is the decision that EAS members have to sign up to the ASEAN Treaty of Amity and Cooperation (TAC) an effort by ASEAN to reassert its central role, or just a clever way to keep Washington (among others) out . . . or both?

- Finally, repeating Secretary Hill's key question, how do members of the East Asian community—whoever they may be—define the relationship between Asia-only mechanisms such as A+3 and broader efforts such as the ARF and APEC? Which type efforts will receive pride of place? Clearly it does not have to be, and is unlikely to be described as “either-or.” But, where will the focus and bulk of the effort be? Will the outcomes and efforts be mutually reinforcing? Will the East Asia effort help set the stage for and supplement or even advance the broader dialogue or will it be used as an excuse for inaction? If the former, how does one create avenues of interaction between East Asian and Asia-Pacific mechanisms to enhance their mutually supporting roles.?

Until the answers to these questions become clear, it will be difficult to determine the prospects for the creation of a true East Asia community and/or Washington's receptivity to this effort.

## 7. An East Asian Community and the United States: A View from ASEAN\*

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### **Introduction**

In December 2005, the first East Asian Summit was held in Kuala Lumpur, Malaysia. While this is a new and quite unprecedented event, it is one that has been considerably, and variously, anticipated and interpreted.

The summit grows from a growing but still nascent sense of regionalism in East Asia, and may both mark and add to the momentum and strength of this sentiment. The path to this first summit has been paved by events in recent years, especially the ASEAN+3 process that has brought together leaders from the ten ASEAN member states with their counterparts from the three Northeast states of China, Japan and South Korea. Indeed, the ASEAN+3 process has grown beyond summitry to provide a framework for initial Asian cooperation on diverse transnational issues such as finance flows, with the Chiang Mai initiative, and public health in the wake of SARS.

For these 13 states, therefore, the East Asia Summit (EAS) would have represented something of a logical next step forward from the ASEAN+3 process. But the attendance at the EAS was not limited to the ASEAN+3 states. It was expanded to include India, and Australia-New Zealand. This expansion was quite deliberately decided, and it both arises from and reflects back on the nascent sense of East Asian regionalism and the relationship of East Asia to the USA. This is especially when we consider that the ASEAN+3 process will continue in parallel with the EAS.

It is in this context that this paper will consider the prospects for an emerging East Asian community, and its relations to the USA.

What is driving the nascent and growing sense of East Asian regionalism? To what ends is the region being driven? What factors in international relations among the states—such as the triangle of US-China-Japan relations, and within ASEAN—can shape the regional architecture?

First, I will examine what would appear to be the main factors that have emerged to drive the current and still nascent sense of regionalism in East Asia, postulating some reasons that some may wish to exclude the USA. Secondly, I will seek to characterize the emergent East Asian regionalism and examine some preferred principles that would allow the most stable and mutually beneficial relationship of this emergent regionalism. Thirdly, I will suggest how the USA might best respond to these developments in East Asia, and what Asians should do, both for the benefit of East Asian regionalism, as well as vis a vis the USA. In so doing, I will glance upon the triangle of relations between the USA, Japan and China, which is a key to strategic outlooks in the Asia Pacific, as well as upon the ASEAN.

While ASEAN cannot be considered a major power, the grouping of smaller to medium-sized states is something of a hub in much of the regional frameworks. I will both describe this role and consider if ASEAN can be a positive influence on the emerging East Asian regionalism as a “soft power”.

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These discussions are necessarily exploratory, given that the EAS and East Asia's regionalism as a whole and a recent phenomena. Positions are still less than fully crystallized. Views differ from one Asian country to another, and have evolved over time. Additionally, US attitudes towards East Asia—which will be major drivers, and perhaps even determinative of the prospects of this phenomenon—are shifting and often seem ambivalent, especially in relation to China.

This is, as such, a situation in which what states and leaders decide to do would matter; in which human agency is very much at play. Thus while conclusions are not easy, we can hope that what can be explored and considered may be make small contribution in informing the policy processes in play. The essay does, as such, offer several policy suggestions to Asians, ASEAN and Americans.

To the Asians, I suggest that we should be prepared to develop closer intra-Asian cooperation on issues of common concern, to deal with both regional issues as well as impacts arising from globalization. However, while we may wish for a rapprochement between China and Japan, this cannot be commanded and there are few signs of a resolution at hand. Without this, I suggest that East Asians must be prepared to be patient and work for the long term, and through a series of patchwork and more limited cooperative schemes, rather than expecting a clear regional vision to be announced and agreed shortly. Therefore, for the near and middle term, East Asia will be more of a framework for cooperation and understanding, rather than a “community”; a word that suggests many more and deeper shared bases and values for coming together.

To ASEAN, I suggest that they must recognize they are presently a hub for East Asia's regionalism and must seize this opportunity to contribute to the process positively. ASEAN's role must however be recognized as resulting from a default in relations among the major Asian powers, and cannot be taken for granted. ASEAN can and should therefore seek to grow into this default role by moving ahead clearly and quite quickly with its ambitions for an ASEAN community, in the fuller sense of that word, “community”. As it does go forward with these ambitions, ASEAN should also seek to emerge as a “soft power” in Asia, with a positive influence arising from the values, norms and institutions that it practices and embodies, as a model for the wider region.

To the Americans, I first suggest that the USA must accept and understand its exclusion from the first EAS and many of the emerging East Asian frameworks. Secondly, all EAS states and especially those who are allies and friends of the USA should seek to ensure that while the EAS does not include the USA as a participant, the vital interests that they share with the USA are sufficiently accounted for and protected. Efforts to convey this to the USA, both as intentions going into the EAS and as results emerging from it, should be redoubled. To Asians and especially Americans, I suggest that we need to work to revive relations across the Pacific and indeed take the existing relationships and institutions to new and higher levels. In this, relations of the USA with states in Asia must broaden beyond the almost singular focus on the global war against terrorism that some feel in dealings with Washington DC and rise above the existing base that provided by the Asia Pacific Economic Cooperation (APEC) and the ASEAN Regional Forum (ARF) processes.

### **Reasons for Regionalism: Neutral or Anti-Americanism?**

Some suggest that regionalism in East Asia is a natural phenomenon that has little to do with the USA and does not demonstrate anti-American sentiment. There is considerable truth in this statement. Regionalism that brings proximate states together to cooperate is not in opposition to the forces of globalization that link all states more closely together than ever, and especially to the USA as the primary economic actor and only post Cold war superpower. Regionalism has been a companion to globalization, and not its opponent. For while globalization connects all states and societies more closely, proximate and neighboring states are more closely connected to each other *inter se*, than to states which further away and/ or are more different in make up.

Globalization is not a complete and neutral phenomenon in this regard. Simple facts such as the cost of telecommunication and transport demonstrate its incompleteness and unevenness. Geography and distance have been reduced as determining and primary factors, but nevertheless do still matter. Cultures and societies too, while being much more open to exchange and influence, persistently resist homogenization. This is true not only in Asia. It is even more clearly visible in Europe and in North America. Regionalism has arisen and thrived in parallel to, and not necessarily in conflict with, globalization. In this view therefore, East Asian regionalism is natural, neutral and indeed long overdue.

Support for this idea of a “neutral” East Asian regionalism is, for example, evidenced by economic data. This witnesses both the predominant place of trade and investment between the USA and Asia, as well as the rapid growth of intra-Asian economic ties. It does not seem to be an either/or situation.

Yet Asia has no strong and enduring history of unity and accepted commonality, whether in polity, culture, language or religion. The antecedents of East Asian regionalism have been brief and contested. One such period was in the 15th century, when the Ming Empire of China ruled the waves and, in the pre-colonial period, extracted acceptance of suzerainty from most of the kingdoms in East and Southeast Asia. A second incident was the Japanese co-prosperity sphere during WWII. Neither sets a happy precedent for East Asian regionalism. Even within ASEAN, after nearly four decades of association, national sovereignty has tended to trump integration in economics and certainly politics. While this has gathered pace, the ASEAN efforts still do not rival—both in aspiration and even more so in reality—the integration of the European Union. As such, we may conclude that East Asia has no precedent in regionalism, and only a limited and very recent movement forward in this direction.

Why then East Asia now?

To understand this, I think it is necessary to go beyond the “neutral” factors that I have briefly canvassed. I would join others in suggesting that less neutral factors are adding to the emergence of an East Asian regionalism that, in some settings and instances, the USA will not be party.

These factors are, in approximately chronological order: first, attitudes toward the USA during and after the 1997 crisis that swept through Asia; secondly, the failure of APEC; thirdly, the need for competent and competitive regionalism in Asia; fourth, the reception of the US security policies, post 9/11; and fifth, the rise of China and the responses among different Asian neighbours.

### ***During and After the 1997 “Asian” Crisis***

The economic crisis that started in mid 1997, spread quickly among almost all economies in East Asia, with little regard to the real differences in their economic fundamentals and little coordinated response by the countries affected. While the crisis has abated, the sense among some in East Asia is that the USA could and should have done more. For example, in Thailand and South Korea (both US allies), negative comparisons were drawn to the level of US assistance to the help given to Mexico when the NAFTA neighbour was earlier struck by a financial crisis.

The role of international financial institutions (IFI), especially the IMF, was also brought into question. While there were no better mechanisms that were readily available, Asians have been among those who argue that many of the prescriptions were ineffective or indeed counter-productive. In the years since the crisis, more have come to share aspects of this view, including well-known US-based economists like Krugman and Stiglitz. Yet efforts at reform and policy changes within the IMF and IFIs are still wanting.

Criticisms of the IMF and IFIs, moreover, rebound on the USA as—rightly or otherwise—some perceive that Washington DC sets and controls the agenda for them. To some of these critics in Asia and elsewhere, the “Washington consensus” is not named innocently for the headquarters of the IMF and World Bank, but bespeaks a consensus shared by the powers that be in Washington DC itself.

### ***The Failure of APEC***

While the Asia Pacific Economic Cooperation (APEC) process continues, there is some sense that it has in some ways, “failed”. This sense of failure comes from at least two sources.

The first, and probably quite unfair criticism, is that APEC failed to respond to the Asian crisis. It is fair to point out that APEC was never intended nor intended to serve such a purpose. But the criticism sticks in some quarters; critics ask that, if little or no response could be made to such a crisis, what is the point of APEC?

The second source of criticism over APEC is perhaps a more measured one. This is that the USA and other major economies have ceased to regard APEC as of being sufficiently important to be used as a mechanism for enabling and managing economic cooperation and integrations between the APEC members. Some would trace this to the impasse between the USA and its close ally, Japan, over trade liberalization measures. Focus on APEC has diminished, as compared to a decade ago. Some now believe that, given the present trajectories, there is little prospect of achieving the APEC Bogor goals by the stated deadlines.

In the wake of these developments, more and more states in Asia and the Pacific have sought to turn to the WTO, only to find delays and faltering there too. Again, impasses relate mainly to the major economies. Only Japan, India and China would have much influence in the WTO negotiations and their positions markedly differ. Thus, the effort to move ahead in the WTO is beyond the influence of many Asian states.

As such, Asians who have tried to find ways forward for economic liberalization have turned to another avenue: regionalism and sub-regionalism. While WTO and APEC remain, greater stock than before is being given to sub-regional and bilateral economic partnerships and trade agreements. Regional agreements include ASEAN’s efforts to implement its FTA (already in force) and move ahead towards an economic community with fuller integration, and “ASEAN+1” FTAs with (separately), China, India, South Korea and Australia-New Zealand. Bilateral agreements also have multiplied, including those concluded between Japan and Singapore, and being negotiated with other ASEAN member states like (separately) Thailand, the Philippines, and Malaysia. A “track 2” experts group has begun to talk about an East Asian FTA. Australia and New Zealand too have not been excluded in this FTA “fever”, with FTAs concluded or in negotiation with Asian states such as China, Singapore, and Thailand.

In contrast, non-Asian states have been relatively less active. Exceptions to this are the US-Singapore FTA, and recently proposed European Union-ASEAN FTA.

Many questions have been raised about the efficiency and efficacy of these bilateral and sub-regional FTAs in Asia as they relate to business and to the actual creation and liberalization of trade. It is true that many are complex, while others are superficial, and all are uncoordinated in respect of their terms so there is no consistency between them. However, in this context, I do not point to their economic use, but rather as evidencing and influencing broader thoughts about regionalism among Asians.

### ***A Competent and Competitive Asian Regionalism***

In the wake of the Asian crisis, Asians have come in these recent years to better appreciate their interdependence. This appreciation has gone beyond the question of financial flows that were implicated in the 1997 crisis.

Other areas such as trade and investment and environmental pollution demonstrate the interdependencies in the region or sub-regions of East Asia. Some examples of this are the haze from Indonesian fires, the acid rain and yellow dust from China that impacts Northeast Asia, and unsustainable and often illegal logging in ASEAN countries to meet the demand of Japanese and Chinese markets (especially since China has banned domestic logging). Public health concerns over SARS and Avian Flu have been other manifestations of the negative face of an increasing interdependence without sufficient governing structures and regimes.

Even in sensitive areas such as violent political upheaval and gross human rights abuses, there is a growing awareness and moral interdependency among many of the people of Asia. While many issues in this area remain off-limits among Asians, sporadic issues such as the crisis in East Timor after the vote of free choice in 1998, and current developments in Myanmar have attracted wide-spread concern among Asians. Institutionally as well, the ASEAN regional forum, which includes non-ASEAN members and covers a wider geographical footprint in Asia, has begun to move into a phase for developing preventive diplomacy among its members.

In toto, whether in economics, environmental or other fields, Asians now give greater recognition to the need for cooperation to manage their existing and still growing integration. Regionalism, in this view, is a process for competently handling globalization and interdependence. It is also a competitive issue among Asians, given parallel developments in Europe and continued feeling that the USA, with or without allies and neighbours, has the weight to determine global matters where its national interest is felt to be involved.

### ***US Security Policies, Post 9/11***

The fourth factor has been the post-9/11 US security policy and its prosecution of a global campaign against terrorism. While there was initial support for the USA across Asia, reactions are not uniform. Some states are staunch US supporters and have been proactive in their own domestic fight against terrorism. Others have been ambivalent and even reticent in responses, preoccupied with their own domestic power politics. Criticism and opposition to the US policies have risen.

Polls and surveys point to this trend across Asian societies, especially in the wake of the US-led “invasion” of Iraq and the revelation of human rights abuses in Abu Gharib and allegations of mistreatment at Guantanamo. Criticism of the US policies among some quarters also relate to wider issues, such as the question of Palestine and Israel.

Such sentiment is strongest perhaps in Asian countries, such as Indonesia, and Malaysia, where there are Muslim majorities. Yet it has grown even in societies where Muslims are only a minority or quite absent. Indeed, in some countries like South Korea—without Muslims and historically intertwined with and dependent on the USA—sentiments among common people about the USA have soured. In many cases, this change in attitude to the USA relates to the US policies not only about terrorism in the global theatre, but its implications in the national and local spheres. America’s post-9/11 agenda has complicated existing internal conflicts and insurgencies in Southeast Asia.

The change in sentiments in Asia towards the USA has paralleled changes in many European societies. However, it would seem that European criticisms more greatly emphasize the questions of human rights and of the observation of international law.

Indeed, while Asian opinions concerning the post-9/11 USA have shifted, there seems to be a considerable difference in the tenor and level of criticism as compared to Europe. Asian states did not join France and Germany in leading opposition to the U.S.-led action.

Public opinion is not the chief difference. As in Europe, there is no strong and widespread domestic support among the peoples of Asia for American action in Iraq. Indeed, in some societies, as noted briefly, anti-American sentiments have risen sharply.

The majority of Asian states have nevertheless continued to support the USA or at least measure and limit their criticisms and opposition, to varying degrees and in different ways. These relate to a realist—if not *real politick*—calculation of the role of the USA in economics and security. There is a calculation of the costs of openly opposing the Bush administration on post-9/11 issues, after the admonition that, “either you are for us, or against us”. There are also some benefits to the governments in the region. In the American post-9/11 agenda, Asia has again received American attention, and Asian governments have generally been quick to respond to align

their interests and agendas to America's. Equally, most have sought to prevent direct interventions into their territories and domestic affairs by cooperating with the United States.

Thus, many Asian governments face an increasing tension between their external commitments to support the United States and these internal views and demands within their societies and among their citizens. While some Asians dissent, this realist logic prevails in thinking that it is best to ally with the United States. Its policies of "benign selfishness" offer the closest match to world interest—the desire for free trade, rule of law, free movement of capital and people, as well as security for persons and property. In this view, stability in Asia may be provided by a hegemonic power, provided it is relatively benign.

However, the prospect of ensuring the US interest in Asia and the world is indeed benign and broadly supported has to contend with a number of factors. Chief among these is that the post-9/11 agenda in the USA responds first and most directly to American domestic opinion (some might say, "only"). This means that there will be severe limits to how much influence other countries, including those in Asia, can have in persuading the US administration in any direction that is contrary to the views of the American voter. American exceptionalism in treaties and multilateral settings illustrates the concerns that Asian and other states have about the dependability and benign character of America internationally.

The necessary corollary of this concern is that Asians should find frameworks to depend less on the USA and also to collectively influence the USA.

### ***The Rise of China***

This brings up the fifth factor that bears mention in context of the East Asian community and the USA: the rise of China. This phenomenon has been long predicted and yet still attracts controversy in interpretation and prediction.

China of late has done much to assure the world and especially the region of its intentions for a "peaceful rise." This has been well received, bar cross-Straits relations, with increased levels of comfort with South Korea and, especially, ASEAN member states. With ASEAN as a grouping, China's initiative in proposing an FTA and deepening its economic and trade ties have been welcome. On the security front, while much remains to be done, the agreement on a Code of Conduct in the South China Seas and a generally more forthcoming engagement with China in the ASEAN Regional Forum and other frameworks have lessened the tensions that once marked the relationship, especially after the Mischief Reef episode.

Questions of course remain. This is especially in respect of relations between a rising China and the USA, as the incumbent and pre-eminent power. Sino-Japanese relations also pre-occupy strategic thinking as well, given both the historical issues and (even more importantly in my view) the present and forward looking issues of accommodating these two giants in the emerging frameworks for Asian regionalism. For the newer ASEAN members, questions over the headwaters of the Mekong, that lie in China, will continue and perhaps grow in coming years.

National differences in Asian's attitudes to China also can be traced to economic competitiveness and prospects of complementarity, as well as to historical differences. There is, as such, considerable variation even among the remaining Asians of how we do and should look at the rise of China (which is worthy of further study).

Notwithstanding this diversity, the rise of China raises two primary issues in the context of East Asian community and the USA. The first of these issues is the ability to imagine an Asia that is less centered on the USA, as it is at present. If the predictions of China's rise prove true, there could be a rebalancing of the economic center for Asia—which still predominately exports to the US market and depends quite considerably on cross-Pacific investment and trade. In politics and security too, there would be changes, with China's promises of a

“multi-polar” world providing a contrast to the existing arrangements that center on Washington D.C. as the hub of various bilateral agreements and alliances.

The second of these issues is connected but different: the need for Asians to proactively pursue ways to engage China and shape its policies towards the rest of Asia. This is especially important if and when the US-China relations grow more competitive and perhaps tense. If so, many Asians would like to have the option of having an independent policy towards China, rather being reflexively aligned to the US position. At the same time, some in the USA may be concerned that such “independence” merely disguises the slip of these Asian states into the orbit of a China that they do not trust.

This issue took on more life in 2005, as we approached the EAS, and have continued to gain pace in some quarters. A number of different constituencies in the USA are raising issues of contention with China, such as the revaluation of its currency, the promotion of democracy and cross-Straits issues and the build up of Chinese military forces. The US policies towards China have changed in tenor from Clinton to Bush, and from early-term Bush to post-9/11 Bush, swinging between the poles of “cooperation” and “strategic competitor”. Of late, in statements such as those by Defense Secretary Donald Rumsfeld, the direction seems to be toward the latter pole of China as a strategic competitor. (I shall survey these concerns slightly more below, in discussing the critical triangle of relations in the Asia Pacific between USA, China and Japan.)

Taken together, the five factors surveyed have created a much greater sense of doubt among Asians toward the USA in its global and regional role than has existed during the Cold War or its immediate aftermath. A strongly “anti-American” sentiment exists but perhaps only among a minority. Asians in responding to the post Cold War order (disorder) in general and post-9/11 Bush in particular, seem to swing between the poles of fearing that the US will ignore them and that the US would intervene unilaterally, at the whims of its domestic audiences. The answer of some East Asians—that we want a sustained, knowledgeable and consultative American engagement—seems an almost impossible wish.

The post-9/11 USA has declined in “soft power” and suasion in Asia, while China has gained in standing and acceptability: thus, the rise of the Chinese dragon is in parallel with the wounding of the American eagle, in a coincidence that may bring misgivings and perhaps sudden shifts. Nevertheless, the main driving forces for the sense of East Asian regionalism are not, in my view, anti-Americanism.

Nor, however, are they completely neutral in my estimate.

There is a growing ambivalence about the USA among more Asians. This “love-hate” attitude finds expression in the now popular adage, “Yankee go home ... and take me with you.” There is an emerging wish for a greater independence and capacity in Asia. More Asians now believe it is the time that their countries and their region mature and grow beyond the unequal relationship with and dependency upon the USA, so that Asians can do about what matters most to Asia.

### **Versions and Principles of East Asian Regionalism**

In surveying the five factors above, I hope that I may not be mistaken to suggest that this is a single or predominant Asian opinion or perspective on the various issues raised. As I hope has been clear, there is a great variety among the Asian states and peoples whether we look at Asian perspectives on the rise of China, the different responses to the US actions and policies after 9/11 or the varied experiences in the Asian crises.

Accordingly, there is no single and agreed vision about the future of East Asia as a region. There is instead a quite broad and even bewildering range of suggestions of what East Asians can and should do together. Some examples include an East Asian Union, a la Europe, and an Asian currency.

I do not wish in this section to canvass the suggestions given to date or to add my own to the considerable and still growing list. Instead, I would like to list some principles that should, in my view, guide the evolution of East Asian regionalism and also to suggest broad directions or versions of East Asian regionalism.

From the observations of the driving forces and limits of East Asian regionalism, several principles may be suggested.

### ***Open and Flexible Caucus***

First, it should be an open and flexible caucus, not an exclusive group or bloc. This is especially given that the United States and other countries may be concerned about being excluded, and the existing reliance of many in the region on the United States for both security and economics. The new East Asian regionalism might therefore serve as a caucus, to discuss and agree on mutually acceptable positions to bring before larger institutions. Indeed, where positions cannot be agreed, East Asian states can and should have the latitude after dialogue to take their own position, and expect that it be understood and respected by its neighbours.

This way, East Asian regionalism would not detract from Asia Pacific and international efforts, but serve to make them more effective and representative. More, the East Asian regionalism can seek out areas of cooperation and begin to build institutional capacity in these areas. In this regard, the ASEAN+3 and EAS are significant markers and can evolve as primary mechanisms, but they should not be the only ones. The evolution of the EAS in terms of the states attending is itself a marker of openness and flexibility needed to move ahead.

### ***Functionality and Interdependence***

Second, East Asian regionalism should have functionality and interdependence, not political fixity, ideology or some easy and false sense of shared civilization. One of the most constructive factors is the need to manage and cooperate in the face of integration and globalization. This emphasizes that the new regionalism should be functional. This will test the tendency to include and exclude members on largely political grounds. An example of this would be in the field of economic and financial cooperation in the region. This has been emphasized in the ASEAN+3 process and also in the EAS, with the inclusion of India and the Pacific-2. If we accept the ASEAN+3 or the newer EAS as a fixed or only structures, then we would exclude important economies such as Hong Kong and Taiwan, in preference to smaller and more isolated economies. The new regionalism should instead be inclusive, with reference to the function that each member can bring to the issue.

### ***Leadership by Issues***

Thirdly, the leadership in East Asian regionalism should be led by issues, and not by great powers. If we look at traditional modes of regionalism, central leadership seems critical, as discussed earlier in the chapter for the need of a benevolent great power. However, without a historical reconciliation between China and Japan, this will not be possible in East Asia. The region lacks a single leader who is acceptable and able. There are suggestions that the small- and medium-sized countries, such as South Korea, and ASEAN might therefore lead the region.

They may have a special and larger role to play than expected, but they cannot offer permanent and strong leadership of the traditional type in the region. East Asian regionalism therefore might have to look at newer and more limited forms of leadership in the region. This could be offered by having leaders on different issues. Leadership would arise from the initiative and interests of different state. This would follow principles of equality more closely than the idea of 'great power' leadership. In this way, the new East Asian regionalism might accord with many of the aspirations voiced in ASEAN and the Asia Pacific.

It is also important that leadership offered in East Asia be one that is benevolent and takes into account the interests of all, especially the smaller and weaker states. If some Asians chaff under the US domination (which had been relatively benign and even helpful for many during the Cold War), they should not come together only to exchange one domination for another.

### ***Coalitions of the Willing***

Fourth, the region should be led by coalitions of the willing (although some new term may be necessary, post-Iraq). The above principles, in total, suggest that East Asian regionalism and its manifestation in the EAS should not be a fixed bloc or union with permanent membership and permanent leaders. Instead it should be a framework for like minded states to caucus and act in coalition. These coalitions can arise from certain issues or even events. They may then dissolve or evolve to new issues. As the need arises they would work with existing regional and sub-regional institutions.

The idea of the EAS has demonstrated this is extending beyond the geographic definition of East Asia, to raft together other countries such as Australia and New Zealand and India. But of course in the created form of the EAS and A+3, where states are agreed participants, the direction of the grouping as a whole needs to proceed at a pace that all can agree to.

### ***Beyond “Asian Values”***

Lastly, in giving voice to regionalism, East Asians should avoid a state-selected version of “Asian values” and identity, as we witnessed in the early 1990s. This had argued that, in then predicted rise of Asia to equality with Europe and North America, Asians could and would legitimately differ in questions of democracy and human rights. Asians would as such be exceptions to what are arguably “universal” aspirations and values. We should recognize that the map of governance in East Asia has changed considerably in the last decade by looking at the developments in the states of the EAS.

In ASEAN, the change in Indonesia post Suharto tipped the scales to make the grouping as a whole much more comfortable with the ideas of democracy and human rights. After all, in addition to the new Indonesian democracy, there are vigorous (if imperfect) democracies in Thailand and the Philippines and voting democracies in Malaysia and Singapore (albeit with dominant parties in place). The ASEAN efforts about Myanmar/Burma may not succeed in changing the regime (and certainly not by ASEAN’s sole efforts), but they do reflect changes in how ASEAN thinks and seeks to promote and to protect basic standards of democracy, human rights and governance.

In Northeast Asia, South Korea and Japan are established democracies. In the wider East Asia, democracy is very much part of the national ethos in India, Australia, New Zealand.<sup>1</sup>

I do not mean to argue here that democracy and human rights can and should be entrenched within what East Asians stand for and collectively should promote. I only mean to argue that defensive and negative attitudes to these ideals, as seen in the earlier Asian values debate, are unwarranted. From this, my more general argument is that East Asians should not rush into declaring any agreed, “Asian values”, lest an artificial, state-led list of such values be foisted on the project. While interactions will increase among East Asians, there are dangers in tying too tightly the ideas of interdependence (especially economic interdependence) with values or morals in a community. We should distinguish between three uses of the idea of increased unity: as interdependence and cooperation; as increasing similarity between the states and societies that are so interdependent and cooperative; and as a consciousness of a shared humanity or culture.

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<sup>1</sup> I have excluded mention of Taiwan, a democracy, as it did not attend the EAS.

East Asians should prefer regional institutions and a growing sense of cooperation and identification with each other, without exceptionalism. Even as Asians cohere more closely, there can and should be interactions with international norms and practices. Globalization and regionalization, as such, are running in tandem, and not as an either/or choice.

### ***Three Models for East Asia***

The principles that I have suggested above stand in contrast to others, as a range among three directions or versions about the possible future of East Asian regionalism. These, for discussion, can be clustered around three “models”.

The first of these would be an “East Asia adrift.” This is much as existed before the ASEAN+3 and EAS processes, and (some might argue) still exists today. While different East Asian states have considerable strengths in economics, security or other fields, the region as a whole offers little synergy and positive interactions. Instead, intra-East Asia engagements continue without much function, energy, leadership or high aspiration. The regionalism remains fragile and indeed fractured. In this version, nothing much happens. Or certainly nothing happens that upsets that present status quo and the USA as the key actor in East Asian affairs.

On the other end of the range of possibilities for an East Asian future is an “East Asian bloc”. In this, East Asians would aspire to a much higher degree of integration, perhaps ala the European Union. However, the East Asian bloc would one that would be closed or even opposed to the USA and other non-Asian states. It might also be based on a fixed set of “Asian values” as perceived by leaders and elites, rather than being more open to global influences, and the aspirations of citizens.

In between these two poles, a third possible version is one that can be described as “East Asian Identity without Exceptionalism”. In this scenario, East Asians develop sufficient processes and institutions to deal with functional interdependence and better recognize an emerging sense of institutional identity. Yet these identities, institutions and processes remain open to influences from other states and from within different societies, and evolve over a longer period, allowing for adjustments.

Some of the principles underlying these three contrasting versions or directions for East Asian regionalism are outlined in the following table:

	<b>East Asia “Adrift”</b>	<b>East Asia “Identity without Exceptionalism”</b>	<b>East Asian “Bloc”</b>
<b>Membership</b>	Focus on ASEAN, and Asia-Pacific processes.	East Asian process, centred on ASEAN+3, but open to USA, others in region and to global institutions	East Asian process, closed and even opposed to USA and global institutions.
<b>Use</b>	Dialogue	Function and interdependence	Ideology
<b>Leadership</b>	ASEAN-led (ARF), US or leader-less rotation (APEC)	Issue-led, including smaller and medium sized powers	Great power leadership and rivalry
<b>Organization</b>	Informal, minimal secretariats and non-binding undertakings	“Coalitions of the willing”, with bilateral, ASEAN and ASEAN+1 processes, and growing institutionalization	Consensus for unified, region wide agreement
<b>Identity</b>	“Pacific Way” with tension between ASEAN and Western approaches	Interdependence and institutional identity	“Asian” Values

Perceptions about ASEAN+3 have warmed both in Northeast Asia and ASEAN. It has also made some useful contributions with the financial swaps arrangement and with the discussion of the SARS outbreak; both demonstrating the usefulness of this framework in preparing for future crisis and even helping deal with present ones. There is some optimism looking forward to the first EAS, notwithstanding the rise in Sino-Japanese tensions, and possible friction in the US-China relationship.

If East Asian regionalism attempts too much it risks opposition from the USA, which may feel that it is being left out from developments that might impact its strategic interests. If so, there are dangers that the US allies and friends might defect from East Asian efforts. American pressure is traced by a number of accounts to the failures of the earlier proposal by Malaysia's Dr Mahathir for an East Asian Economic Grouping and to the idea of the Asian Monetary Fund, discussed earlier. Given the importance of the US to many Asian states, including its allies Japan, South Korea, Thailand and the Philippines, strong US opposition is likely to be fatal to the newer regional efforts as well.

Even left to themselves, East Asians may prefer not to attempt too much, too quickly. The region's historical and on-going divides prevent such commitment and pace. There has, for example, been no rapprochement between Japan and China. There are also questions of developmental divides among the 13 states: the gap between Japan and the Lao PDR, for example, is as stark a gap as any in the world, and far beyond existing gaps in the European Union.

On the other hand, if East Asian regional efforts attempt too little and too slowly, they risk failure and a downward trend in perceptions with time and perhaps the passing of new events. As in the case of APEC, the differences of expectations among members and the failure to respond to crisis may change perceptions from positive to negative.

Between these two dangers, the ASEAN+3 and EAS processes should have to balance different needs and tread something of a middle ground. East Asian regionalism should also be nimble in order to progress. In this regard, we should come to see that the ASEAN+3 and EAS will not, of their own, suffice to bring about an East Asian community. While significant, it is not determined that the ASEAN+3 or EAS will be the only or main mechanisms for East Asian cooperation and community.

Many other institutions and processes can and perhaps will play a part—and often in ways that were not originally imagined. The EAS may well evolve, to include countries that meet its criteria. Some are already proposing Russia and Pakistan to attend the next EAS. There is fluidity in the regional frameworks that we have to expect, and something of an alphabet soup of dialogues and processes. After all, this seems to have been the experience in bringing Europe together, when many institutions other than the European Union played their part. East Asians will need to learn more from those European experiences and adapt (not blindly adopt) them to their own circumstances. There will be a certain experimentalism in East Asian regionalism.

### **Sketching a Region: From A+3 to EAS...and Beyond?**

But even if the frameworks for East Asian regionalism will be experimental, it will still be easier to describe or predict them than it will be to try to answer a more central question: Will the various processes—A+3, EAS or whatever else emerges—be effective? Or will these be epi-phenomenal, without significant and sustained impacts on the region?

In this section, I shall briefly trace the steps in moving to add the EAS to the A+3, and then briefly discuss two underlying factors that can determine the success or failure of East Asian regionalism. The first and perhaps major determining factor is the triangle of relations between the USA, China and Japan. The second and less emphasized factor is, I suggest, the development of ASEAN and its ambitions to become a community.

The original notion of an East Asian Community is traced back to a suggestion by the then premier of Malaysia, Dr Mahathir Mohammed, in 1990. This suggestion was not however taken up with enthusiasm. Instead, it was torpedoed. Links across the Pacific were instead preferred, to include the USA and other partners in the APEC process.

The A+3 process was then launched in the second half of the 1990s, as the first framework exclusively among Asian member states. While this started slowly, it was notable for increasing engagement among the Northeast Asian states, and generating a number of schemes for functional cooperation among the A+3 states. This also revived the echo of Dr Mahathir's suggestion, of a grouping among Asians only.

On this basis, some began to consider the A+3 as a basis for beginning a community among East Asians. A group was appointed by the governments to set out a vision for this community. ASEAN then agreed to hold the first EAS.

As the first EAS approached, the response from the USA to being excluded from Asian summitry has been mixed, and has changed over time. For a considerable time, it seemed that Washington DC did not notice the EAS or did not object to its exclusion. Certainly, the earlier summit meetings among the A+3 leaders elicited no strong opposition from the USA or request to be included.

Yet more soundings from some in the USA in the run up to the EAS indicate a questioning and perhaps quarrelsome attitude to its exclusion. This has echoed early positions of the USA against the East Asian Economic Grouping, mooted by then Malaysian premier, Dr Mahathir Mohammed, even before the formation of the Asia Pacific Economic Community. Some have also been reminded of the US objection to the idea of the Asian Monetary Fund, mooted by some in Japan and the region, during the financial and economic crises that arose in 1997-98. In both cases, a strong American, "No", combined with doubts among some Asian states to derail these initiatives.

Yet, for the EAS, even the allies and closer friends of the USA in the region, such as Japan, South Korea and Singapore, seem to have agreed that the USA should not be included in the first summit. The EAS, unlike the earlier suggestion by Mahathir for an EAEC went ahead. Why?

I suggest this was because of accommodations taken to differentiate the EAS from the A+3 and indeed the earlier EAEC proposal. We should recall that the initial expectation among some was that the EAS would include only the A+3 member states. The major change expected was not a change in who would attend, but that the EAS could be hosted and chaired by one or another of the three Northeast Asian states, and not only ASEAN member states (as is the case with A+3). This would, if adopted, have meant that the Northeast Asian states would be more equal in the process and, given the greater economic and strategic weight of these states, there would be some danger that the Northeast Asian states—China, Japan and South Korea—might come to dominate the EAS.

This was not to be.

Rather than being limited to the A+3 states, the EAS that emerged took the effort to include other states. There was considerable discussion on who should or should not attend the first EAS. Criteria was discussed and finally agreed to decide on states to be invited to the EAS, in addition to the ASEAN+3 states. The criteria includes acceptance of the Treaty of Amity and Cooperation (TAC), a central agreement on interstate relations among ASEAN states and others who agree to it, in relation to ASEAN.<sup>2</sup>

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<sup>2</sup> Many find the TAC uncontroversial in that it reiterates principles of interstate cooperation and the peaceful settlement of disputes that are drawn from the UN Charter. Indeed, to some the TAC has even been criticized as being too bland. Some suggest, however, that the TAC requires neutrality and may run to counter bilateral defence alliances with the USA or other countries. This suggestion is held by some notwithstanding that the Philippines and Thailand, both original TAC signatories, are US allies.

With this, the EAS expanded beyond the ASEAN+3 states and even beyond the geographic notion of East Asia in including India and the Pacific-2 of Australia and New Zealand. The EAS has also agreed that states to host the future summits will, for the present at least, be confined to the ASEAN member states.

The EAS that has eventuated has several characteristics that differ from the original idea of the A+3 evolving to become the EAS and, of course, the older idea of Mahathir for an EAEC. The first characteristic is that ASEAN will remain the central hub of the new summit process. For all its relative weakness, ASEAN is the most acceptable central hub with the region, and the EAS recognizes and consolidates ASEAN's role.

A second characteristic is the effect of the wider membership. To those who feared a possible domination by China in tension with US interests, this offers expectations that the new framework would be more balanced since Australia is a close US ally and US-India ties have grown much closer in recent years, and this adds the US allies of Japan, South Korea, Thailand and the Philippines as well as Singapore (which has a strategic framework with the USA) within the grouping.

A third characteristic is the decision to make the EAS a process that focuses on leaders, with a minimal of scripting and preparatory work by officials. Even when the leaders met, the format was a "1+1" allowing only one other person in the main room with the leader. This has meant that the first EAS has provided a useful and direct exchange among the leaders. It also means that the EAS does not enjoy a fuller bureaucratic system to follow up (or indeed initiate) proposals. One benefit is that the EAS does not, in this regard, attempt to duplicate the A+3 schemes of functional cooperation that have arisen.

A fourth characteristic of the EAS results from the first three. Given ASEAN leadership, the broader membership, and the focus on leaders, we should expect that the EAS will move forward slowly. Indeed, the skeptic may wonder if indeed it will move forward at all.<sup>3</sup>

In addition to these four characteristics of the EAS itself, there are external factors that will impact the progress of East Asian regionalism, and our perceptions of this phenomenon. Two key factors are, first, the great triangle of relations between the USA, China and Japan; and, secondly, the developments within ASEAN.

### ***The Great Triangle***

It is not possible for this essay to do justice to the fuller considerations of the great triangle of relations in the Asia Pacific between the USA, China and Japan, or even to any single leg of this triangle. It is however important to sketch some of the ways in which this triangle impacts on East Asian regionalism.

Where the triangle is stable, and relations among these three major powers is relatively settled, East Asian regionalism is unlikely to be seen as a possible threat by the USA, or cause fear of American exclusion. Conversely, where relations within the triangle are tense, this possibility is increased. The prospects of East Asian regionalism are therefore affected by changes in the great triangle.

This is perhaps most clearly seen in the US-China relationship. This relationship has gone through various ups and downs during the Bush administration alone. At present, it seems to be heading towards an increased sense of competition and tension. There are economic issues such as the trade surplus and question of the value of the Yuan. There are security issues such as China's rearmament, as strongly raised by US Defence Secretary Rumsfeld, as well as the question of cross-straits ties. There are perennial questions about democracy, human rights and standards in environmental protection and labour rights. As a whole, some might feel that there is broad, if strange, coalition of Americans against China: from the union-friendly freeing the loss of

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<sup>3</sup> Looking forward, some now suggest that countries like Russia and Pakistan should join in the EAS. This remains to be agreed. If the EAS is expanded to include these states, some fear it may become (more) unwieldy.

competitiveness and jobs, to the hawkish right wingers, through to those advocating democracy and human rights abroad.

On China's part, there is also a segment who believe that a confrontation with the USA is inevitable over these issues or, more generally, simply because the world has not known the peaceful co-existence of two great powers. They see the US structure of alliances—both old as well as post-9/11—as efforts to encircle China, not only in East Asia but also in Central Asia and much of the world. Such thinkers may therefore be supportive of China's current “charm offensive” and talk of its “peaceful rise”. But for them, unlike others, these are not as permanent foreign policy, but only ways to win friends and political space and time for the time being, as the country grows and strengthens.

How does this impact the rest of East Asia? Looking at this US-China leg of the triangle, some would trace one of the reasons for the inclusion of Australia and India for the EAS, as compared to the A+3. In the A+3 process itself, we may recall that when the process started, the USA felt relatively comfortable while it was China that showed some initial resistance. Some among the Chinese expressed concern that the A+3 process was aimed by the rest of the Asian states at corralling China, like Lilliputians trying to tie down Gulliver. China's emphasis, at that point, was to prefer bilateralism in its dealings with Asian states, notably in relation to conflicting claims with different ASEAN member states over the South China Seas. However, more recently, China seems too much more comfortable and indeed supportive of the A+3, and has also embraced intra-Asian multilateralism. On the still fraught question of the South China Seas, it has supported a code of conduct among the claimant states. China has conducted a very successful “charm offensive” and increased its influence among Asian states, including most in ASEAN. Thus China has warmed to the A+3 process and has come to engage actively and prominently in the framework. Indeed, its presence in the A+3 has been so strongly felt that some have feared that, again like Gulliver, China would not just burst the bonds tied by the Lilliputians, but pull them along at the end of the string.

How China responds to the EAS framework remains to be seen. But at present, my reading is that China will go along with the EAS but is expecting that the A+3 will remain the more important and functional regional framework. This view is also taken in a number of ASEAN member states, including Malaysia who hosted the EAS and has developed close relations with China.

The growing regional role and influence of China has impacted another leg of the great triangle, between China and Japan. Sino-Japanese relations have remained poor and indeed grown more tense in recent years. The visits by Japanese premier Koizumi to the Yasukuni shrine, and the protests in response to the visits, are emblems of this, with violent protests in the streets of China and a diplomatic impasse to high-level meetings. Worse, simmering beneath the shrine visits are wider and deeper differences about war time issues, and history books. Looking ahead, the view is bifurcated. On one hand, the economic figures of trade and investment show deep complementarities between the two economies, for mutual benefit. On the other hand, there appears to be some danger of a political competition and even conflict, underscored by China's efforts to strength her military forces and develop its maritime capabilities, in tandem with Japan's seeming wish to be a “normal” country with an unabashed military capacity. Nationalism in both countries seems to be resurgent and may be of a narrow, nastier type in some quarters.

These difficulties in Sino-Japanese relations matter a great deal to the project of East Asian regionalism. East Asian regionalism would gain tremendously if these two Asian giants could come to a rapprochement, akin to the French-German partnership that drove European integration. East Asian regionalism can survive and proceed (albeit with some uncertainty and less pace) if Sino-Japanese relations are cool. But if Sino-Japanese relations turn sharply for the worse—to a frosty cold or even boiling over—this could disrupt the early beginnings of East Asian regionalism.

In recent years, ASEAN member states have seen a form of positive competition between the two giants in relation to them, as China and then Japan have come forward to offer FTAs and forms of assistance. But this sense of positive competition may be turning for the worse. When we look at Japan's ties to ASEAN member states and to its nearest neighbour, South Korea, we may have to conclude that Japanese influence in the region seems to have ebbed in a number of respects, despite its continuing largesse to many of the states in the region.

Given this, Japan seems to have faced something of a choice in its foreign policy priorities: whether to continue and intensify its efforts to strengthen relations with the rest of Asia, or to re-prioritise its relations with the USA and a more global role, in tandem with the USA. While perhaps the choice is never as stark or clear, there are signs and statements by Japanese leaders that they have chosen to re-prioritise their alliance with the USA. An alliance once described as being adrift by the well known Japanese commentator, Yoichi Funabashi, has now been celebrated by both American and Japanese leaders as a key priority.

There are those who expect that, as such, Japan will begin to play a larger role in global affairs, including peace keeping and the use of its military power. If this characterization of Japanese policy choices is correct, this has a strong impact on the prospects of an East Asian regionalism that, while not being anti-American, is more independent of the USA than it is presently.

### ***What Can ASEAN Do?***

In its near 40 years of existence, ASEAN has had its share of both critics and lovers. Criticisms mounted especially after the 1997 financial crisis when the grouping was unable to cooperate to address the cross-border flows that affected so many of its member states, and also stood to one side on political and security issues, such as the separation of East Timor from Indonesia. There was a sharp fall in ASEAN's standing. In the years since, the rise of China now occupy many more minds than the happenings in ASEAN. So too does India. A visible sign of this was the decision by US Secretary of State Rice in 2004 whose first tour of Asia was marked by a visit to India and then to China, leapfrogging over Southeast Asia. In that same year, she skipped the annual ARF.

In 2006, almost a decade after the crisis, how should we look at ASEAN? Is it a central and influential player in Asia and the Pacific, or a powerless, marginal association? Has ASEAN responded to the challenges of these recent years, and what direction do these responses signal for the grouping?

There was an initial denial in some quarters that ASEAN needed to respond and change to the challenges of globalization, as revealed in the 1997 crisis and its aftermath. However, more and more ASEAN leaders and policy-makers have come to recognize that changes are needed. Changes are afoot within ASEAN. These will evolve the "ASEAN way" and modes of cooperation among its member states. Indeed, these changes will, if carried through, transform the grouping. These changes, moreover, are important not only to ASEAN member states and their peoples as "internal" issues to ASEAN. Potentially, these changes will also have "external" consequences, to impact ASEAN's standing and its ability to influence the relations among major powers in the wider region.

ASEAN leaders at their summit in 2003 declared their ambition to create an ASEAN community. This community will feature three pillars—in the spheres of economics, security and socio-cultural affairs—that are presently being discussed and defined. The leaders have also commissioned an eminent persons group (EPG) to consider an ASEAN Charter. These initiatives have been followed up with discussions and plans among ASEAN officials. There is an understanding that grouping must go beyond the ASEAN Free Trade Agreement (AFTA) towards greater economic integration. ASEAN Defence Ministers met in 2006, for the very first time. The Charter EPG has met thrice and expects to deliver its report by end 2006.

The ASEAN skeptic can of course point out that these are merely meetings, with no clear cut deliverables to date. This is true. However, those watching ASEAN more closely may discern a difference in the level of ambition, and the conception of ASEAN. The agreement to move towards “community” is not banal, but represents a quite radical change in conception for ASEAN, which for so long was seen and defended as an “association”. The differences between these concepts of “community” and “association” are considerable, and portend fundamental changes in how the ASEAN member states cooperate, and to what ends they should cooperate. A new direction has been set.

The pace in which ASEAN can move in this new direction remains to be seen. Given the diversity of its member states—in economics, political systems, culture and experience with the wider world—it will likely be difficult to move quickly. However, the political will among most ASEAN member states to make those changes is now higher than it has been before. There is more effort and thinking about making ASEAN’s workings stronger and more efficient. Issues are being considered, like the norm of non-intervention, the weakness of the ASEAN secretariat, and the lack of development assistance and transfers amongst ASEAN member states.

The need for ASEAN to go beyond official circles is also more recognized. Consultation with non-governmental organizations, with businesses and with national Parliaments is beginning to change the circle of voices that guides developments in the region. Even more, efforts are beginning to reach out to the wider publics in the member states; to make ASEAN better known to the peoples.

These internal changes represent a quite radical rethinking about ASEAN; not just by intellectuals and observers, but also those who are in power, and advising governments. Before the crisis, most ASEANists disregarded European models of community building as being unsuitable and unnecessary. Today, there is more interest in learning from other regional experiments, even if the mandate is to adapt and not to blindly adopt. We should expect that ASEAN will change, more quickly than in the past, even if not fast enough to satisfy some.

As such developments unfold, ASEAN will move towards what some scholars have termed, “legalization”—with norms and rules that are agreed and then are monitored for compliance. This does not necessarily mean that ASEAN will become as institutionalized and legalistic as some other regional groupings, like the European Union. Nor will the ASEAN secretariat and organs be transformed overnight into autonomous bodies like the European Commission. But these trends in the increased importance of rules, institutions and rule compliance suggest a marked shift from previous ASEAN habits of informality and having very minimal institutions. This is important work not only for ASEAN in itself, but for the grouping’s potential in influencing regional order.

The changes outlined above promise to transform ASEAN internally. They also potentially affect how ASEAN relates to other powers in the wider region. It has been an oft-declared ambition for ASEAN to be in the driver’s seat for such relations; this aspiration remains in that place in the ARF. Doubts however have emerged in the past years of the crisis about the ability and indeed the credibility of ASEAN in this role. Bilateral ties with the USA have been reinforced. The rise of China and its influence has also been marked and some believe that it will seek to play a larger and perhaps dominant regional role. Others, looking at the continuing role of Japan and the rise of India, suggest the rise of a concert of powers to accommodate the different Asian powers.

Some believe that, in this context, ASEAN is doomed to be a marginal presence. Yet, while it is true that ASEAN cannot and does not harbor ambitions to contend for power, ASEAN is presently a default hub for relations in the region. Looking forward, I would argue that ASEAN can indeed be a significant player as a “soft power” in the region. This conception of “soft power”, first developed by Joseph Nye, defines the ability to influence and achieve one’s ends, even without the raw calculations of military strength and of economic prowess.

ASEAN's present place as a hub in the region is marked by three phenomena: the free trade agreements in Asia; the ASEAN+3 process; and the East Asian summit. These are limited to Asian states and possibly offer the beginnings of a regional order that gives expression to a nascent Asian regionalism.

The evolution of free trade and economic agreements among Asians is an example of this. The offer by China to ASEAN for a free trade agreement (FTA) may be seen to be a major impetus for Japan to go beyond the economic partnership agreement that it concluded with Singapore (the JSEPA), and reach out to some ASEAN member states with bilateral FTAs. After initial agreements with the Philippines, Thailand and Malaysia, it is expected that Japan will also negotiate a wider FTA with ASEAN as a whole. These FTA developments have, in turn, played a part in influencing South Korea to begin a negotiation with ASEAN. Taken together with ASEAN negotiations with Australia-New Zealand, and with India, we may surmise that ASEAN has become a default hub for economic relations among the Asian states.

While some or much of this may result from the rivalries between China on one hand, and the USA, Japan and US surrogates on the other, there are positive aspects of these developments for both ASEAN, and (arguably) for the wider region. For rather than splitting ASEAN and the region into two spheres of influence, thus far, these developments have helped East Asia take steps towards closer economic cooperation and integration – albeit in a patchwork manner, rather than a grand design for community or union. The evolution of the EAS is imprinted by these same factors. As discussed earlier in this essay, the EAS re-emphasizes the central position for ASEAN to play in regional order, as a grouping most acceptable to all.

However, ASEAN must recognize the role it currently occupies is a default role. ASEAN is in the centre not because of its intrinsic and irreducible strength or worth but because there is no other acceptable actor. In some senses, ASEAN's main "strength" is its relative weakness and neutrality. While ASEAN enjoys this hub status, it should avoid choosing between aligning itself with one major power or another, either broadly or (worse) permanently.

ASEAN should increasing work towards sharing perspectives towards the major powers and developing common stances in their relations. This is ambitious, given the diversity among ASEAN member states in their economic, political and cultural outlooks. But steps in this direction are not impossible; this is especially true if we accept that the common points among ASEAN member states need not be comprehensive to cover all issues in advance, and instead seek to develop them more organically, in response to new undertakings and events. For example, in the negotiation of the ASEAN-China FTA, ASEAN member states are finding that, despite and because of their differences, they do best to sit down together to discuss and understand each other's positions before responding to China. Other examples show the possibility and strength of common agreement on political and security issues: ASEAN's common stance on China after the Mischief Reef incident in the early 1990s, and of course, the unity of the then ASEAN member states in pursuing their political campaign against the Vietnamese occupation of Cambodia. In like manner, if ASEAN member states can confer amongst themselves on vital issues concerning the major powers, on a timely basis, they can similarly seek out shared positions that may well accommodate their diversity, and better advance their common interests; somewhat akin to a limited form of a common foreign policy.

In this way, ASEAN should aim to emerge as a "soft power" in the region, whose norms, values and institutions are admired as being acceptable and indeed something of a model for the region. Thus far, ASEAN's relations with the major powers in Asia (and indeed with each other) have predominantly been viewed through the optic of realism and calculations of power. But this must change in the future and be complemented by a greater recognition of the potential role of ASEAN as a "soft power",

ASEAN is working towards greater integration among its member states and, in the process, reviewing its norms and institutions for cooperation. We must expect that, in a number of areas, especially concerning

ASEAN economic integration, rules and rule enforcement within ASEAN will be more greatly emphasized than in the past. The institutions of ASEAN, including the ASEAN secretariat and the meetings of the senior officials, will also need to be consolidated and focused to be more efficient and effective. It is critical that ASEAN must emphasize and work towards ASEAN community, the “internal” goal discussed earlier.

These internal and external changes and challenges intertwine for ASEAN. The role for ASEAN in the region cannot be predicated on calculations of power. Rather, if ASEAN is to influence the region, its contributions and role will be in the nature of developing norms and institutions for the wider region. Part of these will inevitably draw from ASEAN norms and modes of cooperation. For example, in the coming together of the EAS, each attending state was required to have accepted the ASEAN Treaty of Amity and Cooperation. This exemplifies the ability and use of having ASEAN serve to guide the regional development in terms of its norms and values.

However, while ASEAN ways may be commended for the wider regional order, they cannot and should not be commanded. Indeed, ASEAN must recognize that its own modes and norms are evolving, and remain open to change and improvement. This often reflects the internal changes within ASEAN member states. For instance, the emphasis that ASEAN has brought to bear on the domestic situation in Myanmar is not merely reflective of the downward trend in that country. It also reflects the upsurge in the ethos of democracy among some other member states, especially in post-Suharto Indonesia. This emphasis on democracy would have been unimaginable in the pre-crisis ASEAN. It demonstrates how ASEAN is evolving and incorporating new norms and values into its expectations for its member states and how they are to cooperate with each other.

Such an evolution stands ASEAN in good stead. The potential contribution of ASEAN lies not in trying to balance power with power in Asia. ASEAN’s potential in influencing the regional order lies instead in a renewed form of “open regionalism” with norms and values, and the development of ASEAN “soft power” in handling its own region and also providing possible models for wider regional cooperation and order.

## **How We Should Respond**

Based on the observations offered above, I shall now turn to some policy recommendations for those Asians in the EAS, for ASEAN, and for the USA.

The future of East Asian regionalism and community does not lie, however, exclusively within Asian hands. Given the role of the USA in the region, what it does and how it responds is important and indeed critical to the emerging regionalism. There is some sense that East Asian regionalism has come this far, towards the first EAS, because Washington DC did not notice it, or if it did, that it was comfortable that its primary interests would not be adversely affected. Otherwise, some believe, that an American “veto” would have been exercised, as it was against Mahathir’s proposal for an East Asian Economic Grouping.

During the ASEAN+3 processes, US suspicion and antagonism was largely avoided. This is due, in part, to the pre-existing APEC framework that has not been displaced by the ASEAN+3. Another positive factor was the generally supportive attitude of most East Asian countries to the USA, post-9/11, despite the sentiment of some of the peoples of the region. A third factor was that the USA seems to have been preoccupied and, if indeed Washington DC’s thinkers considered the prospects of East Asian regionalism, thought it very limited. This appears to be changing with the EAS. While American interest in East Asia is critical and much wanted, a sense of alarm and American opposition to the EAS and East Asian community are unwarranted and would be counter productive.

The USA can legitimately rely on its allies and friends in the region to ensure that its/ their vital interests are not compromised by whatever might happen at the EAS. Indeed, all of East Asia would be well served if such bilateral dialogues between the USA and its Asian allies like Japan, Australia, Thailand, South

Korea and the Philippines, and other close friends like Singapore, would be energized and directed towards a dialogue on the EAS and underlying issues and factors in East Asian regionalism. In this, I would hope that Asian perspectives on the five factors that this paper has surveyed might be conveyed to the USA. This is especially as regards different and varied Asian perspectives on the rise of China, and on America's policies, post 9/11.

We should however have caution over what might be called, "excessive bilateralism" in which one or more US allies and friends would be seen (or see themselves) as surrogates to protect any and all US interests to the point that it might up-end the East Asian efforts at going forward. One sign of such "excessive bilateralism" has been the suggestion that the US will engage in military training with Japan and Australia, which some have regarded as a warming up of a potential alliance to counter and contain China. To be a useful friend to the USA in Asia, these states will have to realize that they must be *in and of Asia*, as much as to be a US friend.

Having said what I hope the USA will not do, what positive suggestions can be offered? Given my argument that the ASEAN+3 and EAS cannot be the only mechanisms, I would point to the possibilities of increasing and deepening US engagement with East Asians in different forms. Two existing processes that deserve greater attention and effort are APEC and the ASEAN Post Ministerial Dialogue with the USA.

In asking that we relook at APEC, we should be reminded that APEC itself initially represented a change in US policies. In the 1990s, there was a policy shift for the US, through then Secretary of State Baker, to express support for a new Asia Pacific architecture, which would comprise a framework for economic integration, a commitment to democratization, and a revamped defense structure for the region. The Clinton administration embraced the concept of multilateral security dialogue as one of the four pillars of the 'new Pacific community', and expressed support for several potential areas of dialogue including APEC.

There were several considerations that contributed to Washington's appraisal of policies and APEC, but none was more important than the prediction that US power could no longer perform the coordinating role characteristic of the Cold War period. The assessment by many in this period was that the two traditional pillars of American predominance in Asia—the American wallet in the form of its markets and overall financial presence, and the US security muscle from its bilateral alliances and military bases—were both diminishing assets.

This possibility has thus far remained unproven. Indeed, the past decade seems to have gone in the opposite direction, with the USA emerging as the pre-eminent power.

Nevertheless, I would argue that APEC needs to be re-energized as an overarching relationship with Pacific Asia (ASEAN, Northeast Asia, the Pacific-2 of Australia and New Zealand and India). This would be a good forum to address trans-Pacific issues, to place China-US relations in a broader context, and also to serve as a safety net in the event that, as was earlier predicted, traditional sources of American influence—of its economic wallet and its security muscle—should wane. APEC's broad agenda of cooperation can also be useful for the USA to demonstrate a much broader engagement with Asia, beyond the sometimes singular focus on terrorism and security.

Some have already suggested that the USA needs to be more mindful of public relations and perceptions in East Asia. I would go further to suggest that a real dialogue about US policies and their communication is needed, to guard against unintended consequences and the continued reduction of their "soft power" to influence and persuade, and serve as an example to be admired and emulated.

In re-looking at the ASEAN-US post ministerial conference, Americans sometimes wonder why they should bother at all with a grouping of ten smaller to middle sized countries. Terrorism post 9/11 has provided something of an answer and reason for American attention to the region. But terrorism is also proving a narrow lens that obscures as much as it reveals.

One thing that seems to have been obscured is the relative importance of ASEAN in East Asian regionalism. In addition to the ASEAN+3 process, it should be noted that ASEAN is the hub for trade and

economic ties. There are also separate spokes under negotiation to link it to China, Australia-New Zealand, and India, as well as discussions of links to Japan and to South Korea. Much of this has been possible not because of ASEAN's strength—whether economic or in terms of security. Rather, it has been because of ASEAN's political acceptability in providing a relatively neutral and positive hub to many different states in Asia.

Additionally, Some ASEAN member states like Singapore and Thailand have also shown themselves to be capable of taking initiative through bilateral agreements and then helping steer the rest of ASEAN in the same direction. ASEAN's own integrative efforts towards an economic community, and with security and socio-cultural communities coming after, also bear mention.

In this regard, it would serve the USA well to engage ASEAN more fully and in more rounded perspectives as a means of remaining engaged and vital to East Asian developments. A free trade agreement with more ASEAN member states or with ASEAN as a whole would be one policy option. At present, the USA has only concluded an FTA with Singapore.

Another suggestion would be to have an ASEAN-US summit, regularly if not annually. China, Japan and others in East Asia already have such arrangements with ASEAN. I have previously suggested that, in part, this can be achieved on the sidelines of the APEC Summit as seven out of the 10 ASEAN member states attend the APEC Summit (from the US point of view, it is politically significant that Myanmar/ Burma is not one of them). This eventuated in 2005, in the months before the EAS. At the very least, this practice should be continued, with the prospect of a full summit for the future.

In sum, to the Americans, I would make the following suggestions. First, the USA must accept and understand its exclusion from the first EAS and many of the emerging East Asian frameworks. Secondly, all EAS states and especially those who are allies and friends of the USA should seek to ensure that while the EAS does not include the USA as a participant, the vital interests that they share with the USA are sufficiently accounted for and protected. Efforts to convey this to the USA, both as intentions going into the EAS and as results emerging from it, should be redoubled. To Asians and especially Americans, I suggest that we need to work to revive relations across the Pacific and indeed take the existing relationships and institutions to new and higher levels. In this, relations of the USA with states in Asia must broaden beyond the almost singular focus on the global war against terrorism that some feel in dealings with Washington DC and rise above the existing base that provided by the Asia Pacific Economic Cooperation (APEC) and the ASEAN Regional Forum (ARF) processes.

It is not however only the USA to whom I would offer policy suggestions in proceeding with East Asian regionalism. Asians and ASEAN too have responsibilities to undertake.

To the Asians, I suggest that we should be prepared to develop closer intra-Asian cooperation on issues of common concern, to deal with both regional issues as well as impacts arising from globalization. However, while we may wish for a rapprochement between China and Japan, this cannot be commanded and there are few signs of a resolution at hand. Without this, I suggest that East Asians must be prepared to be patient and work for the long term, and through a series of patchwork and more limited cooperative schemes, rather than expecting a clear regional vision to be announced and agreed shortly.

Therefore, for the near and middle term, East Asia will be more of a framework for cooperation and understanding, rather than a "community"; a word that suggests many more and deeper shared bases and values for coming together. East Asians will need a vision of their future, but they will also need pragmatism and patience in their efforts to achieve those visions. Practically applied, East Asians may well have to accept that major "hard security" issues such as the cross Straits issue and North Korea will be beyond East Asians for the present and foreseeable future, and be slower and more diffident in approaching issues of political and security concerns.

East Asians may wish instead to focus on issues of functional cooperation and economic agreements. These are of no lesser importance in many ways. Indeed, given different conceptions of security, if East Asians can cooperate effectively on issues such as preventing a new financial crisis or pandemics, and dealing with major natural disasters like the Tsunami and the earthquake in Java, these are arguably contributions that will benefit ordinary Asians in ways that are as important (if not more so) than the hard security issues. If East Asians wish for more ambition, their attention and cooperation in the middle term might turn to issues such as Myanmar—which would centrally involve India and China alongside ASEAN—or Timor Leste.

To ASEAN, I suggest that they must recognize they are presently a hub for East Asia's regionalism and must seize this opportunity to contribute to the process positively. ASEAN's role must however be recognized as resulting from a default in relations among the major Asian powers, and cannot be taken for granted. ASEAN can and should therefore seek to grow into this default role by moving ahead clearly and quite quickly with its ambitions for an ASEAN community, in the fuller sense of that word, "community".

As it does go forward with these ambitions, ASEAN should also seek to emerge as a "soft power" in Asia, with a positive influence arising from the values, norms and institutions that it practices and embodies, as a model for the wider region. The ASEAN processes and institutions, and the ASEAN Regional Forum, must be strengthened accordingly. ASEAN member states must also continue to strengthen their habits of dialogue on issues on which they will face differences and seek to find more common positions and indeed policies in respect of important issues in their relations with the major powers. The national interests of each ASEAN member state does not need to be abandoned, but skilful diplomacy and some degree of restraint will be needed to bring ASEAN closer together and make it more effective in the wider region.

### **Conclusion: Visions, Contingencies and Assurances**

Some hanker for a longer-term vision or roadmap for East Asian regionalism. This is not notwithstanding the fact that an East Asian Vision Group, formed by experts and eminent persons, has concluded its work some years ago with a broad report. Like Europe, they hope for politicians and others to give regular affirmation to an ideal of union, of community, or some other form of deeper association and integration in the region.

There are very real limits to a realism that is bereft of ideals and broader visions and values. Yet I would argue that ideals, visions and values in East Asia should be more appropriately developed over the longer term, rather than concocted here and now by governments or their surrogates.

There are doubts, contestation and differences among East Asian members that I have touched upon and that cannot be wished away. Given this, if we were to attempt another vision, the vision would in some ways be captive to these differences. As such, rather than a vision that might unify the governments and peoples of the region, it may instead divide them.

A hasty declaration of visions, values and ideals for East Asian regionalism may also unnecessarily upset relations with the USA. This is not just an issue for those in the region who are friends and allies of the USA, but also for those whose relations remain in balance, or are in flux.

For much that is happening in East Asian regionalism is necessarily contingent and contested. This is not only the situation within and among Asians, with different histories, priorities and hopes. The sense of contingency and contestation is also present when we think, as we must, of the relations between a more institutionalized East Asian process and identity and the USA, which has been for so long and is still in many respects the predominant pillar of the region, even if it is not physically part of it.

What we should therefore seek to offer in the near term, over the next few years, is not a new vision of East Asia or a categorical decision about Asia-American relations. Assurances instead should be offered.

These assurances relate to the principles for East Asian regionalism that should be preferred—such as its openness and functionality—as well as to the willingness and even fond wish to broaden and deepen engagement with the USA in parallel to East Asian regionalism.

Such assurances do not of course settle things for the long term. However, I hope that if given and taken, such assurances would allow the emerging and still nascent sense of East Asian regionalism to go forward with an America that is not watching as an outsider in alarm or opposition, nor ignoring these developments. Rather, with these assurances, Asians can hope for an America that is fully engaged and watchful with both anticipation and awareness that if things go right, East Asian regionalism can better serve both Asia and US engagements in Asia.

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## 8. (1) Program

### The 2<sup>nd</sup> International Workshop on “An East Asian Community and the United States”

June 20-21, 2006

Sponsored by the Council on East Asian Community (CEAC)  
Co-Sponsored by the Pacific Forum CSIS  
Supported by the Japan Foundation Center for Global Partnership (CGP)

#### Tuesday June 20, 2006

17:30 Registration “Aries”, 37<sup>th</sup> Floor, ANA Hotel Tokyo

18:00-20:00	Welcome Dinner hosted by Prof. ITO Kenichi, President, CEAC
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#### Wednesday June 21, 2006

International Workshop “Conference Room,” the Japan Forum on International Relations, Tokyo

9:15-9:45	Opening	<b>Workshop Objective and Overall Assessment</b>
	<i>Opening</i>	Prof/Amb. ISHIGAKI Yasuji, Vice President, CEAC
	<i>Introductory Remarks (15 min)</i>	Prof. TANAKA Akihiko, Professor, the University of Tokyo
	<i>Introductory Remarks (15 min)</i>	Mr. Ralph COSSA, President, the Pacific Forum CSIS
9:45-10:35	Session 1	<b>Emerging East Asian Community? - Political Process (Chapter 1)</b>
	<i>Moderator</i>	Prof. TANAKA Akihiko
	<i>Presenter (10 min)</i>	Dr. JIMBO Ken, Senior Research Fellow, the Japan Forum on International Relations (JFIR)
	<i>Commentator (10 min)</i>	Dr. Prapat THEPCHATREE, Chair, ASEAN Studies Program, Institute of East Asian Studies, Thammasat University
	<i>Commentator (10 min)</i>	Prof. Jae Ho CHUNG, Professor and Chair, Department of International Relations, College of Social Sciences, Seoul National University
	<i>Free Discussions (20 min)</i>	All Participants
10:35-11:25	Session 2	<b>Economic Integration in East Asia: Trade (Chapter 2)</b>
	<i>Moderator</i>	Prof. TANAKA Akihiko
	<i>Presenter (10 min)</i>	Prof. URATA Shujiro, Professor, Waseda University
	<i>Commentator (10 min)</i>	Dr. Charles MORRISON, President, the East-West Center
	<i>Free Discussions (30 min)</i>	All Participants
11:25-12:15	Session 3	<b>Economic Integration in East Asia: Financial and Monetary Development (Chapter 3)</b>
	<i>Moderator</i>	Mr. Ralph COSSA
	<i>Presenter (10 min)</i>	Prof. SHIRAI Sayuri, Professor, Keio University
	<i>Commentator (10 min)</i>	Prof. URATA Shujiro
	<i>Free Discussions (30 min)</i>	All Participants

12:20-13:20	Business Lunch	Seventh Heaven (Chinese Restaurant)
13:30-14:20	Session 4	<b>Political and Social Integration in East Asia? (Chapter 4)</b>
<i>Moderator</i>		Mr. Ralph COSSA
<i>Presenter (10 min)</i>		Dr. FUKUSHIMA Akiko, Director of Policy Studies and Senior Fellow, National Institute for Research Advancement (NIRA)
<i>Commentator (10 min)</i>		Dato' Mohamed JAWHAR Hassan, Chairman and CEO, Institute of Strategic and International Studies Malaysia
<i>Commentator (10 min)</i>		Mr. Simon TAY, Chairman, Singapore Institute of International Affairs
<i>Free Discussions (20 min)</i>		All Participants
14:20-15:10	Session 5	<b>Cultural Diversity and an East Asian Community (Chapter 5)</b>
<i>Moderator</i>		Mr. Ralph COSSA
<i>Presenter (10 min)</i>		Prof. AOKI Tamotsu, Professor, Waseda University
<i>Commentator (10 min)</i>		Dr. Edy PRASETYONO, Head of Department of International Relations, Centre for Strategic and International Studies (CSIS)
<i>Commentator (10 min)</i>		Prof. Jae Ho CHUNG
<i>Free Discussions (20 min)</i>		All Participants
15:10-15:25	Coffee Break (15 min)	
15:25-16:15	Session 6	<b>An East Asian Community and the United States: US View (Chapter 6)</b>
<i>Moderator</i>		Prof. TANAKA Akihiko
<i>Presenter (10 min)</i>		Mr. Ralph COSSA
<i>Commentator (10 min)</i>		Dato' Mohamed JAWHAR Hassan
<i>Commentator (10 min)</i>		Dr. Charles MORRISON
<i>Free Discussions (20 min)</i>		All Participants
16:15-17:05	Session 7	<b>An East Asian Community and the United States: East Asian View (Chapter 7)</b>
<i>Moderator</i>		Prof. TANAKA Akihiko
<i>Presenter (10 min)</i>		Mr. Simon TAY
<i>Commentator (10 min)</i>		Mr. Ralph COSSA
<i>Commentator (10 min)</i>		Dr. Edy PRASETYONO
<i>Free Discussions (20 min)</i>		All Participants
17:05-17:55	Wrap-up Session	<b>General Discussions</b>
<i>Co-Moderators (10 min)</i>		Prof. TANAKA Akihiko
<i>Co-Moderators (10 min)</i>		Mr. Ralph COSSA
<i>Free Discussions (30 min)</i>		All Participants
18:00-20:00	Working Dinner hosted by Prof. TANAKA Akihiko (Lawry's The Prime Rib)	

## 8. (2) Participants List

### <Indonesia>

Dr. Edy PRASETYONO Head of Department of International Relations, Centre for Strategic and International Studies (CSIS)

### <Japan>

Prof. TANAKA Akihiko Professor, the University of Tokyo

Prof. AOKI Tamotsu Professor, Waseda University

Dr. FUKUSHIMA Akiko Senior Fellow and Director of Policy Studies, National Institute for Research Advancement (NIRA)

Prof. URATA Shujiro Professor, Waseda University

Prof. SHIRAI Sayuri Professor, Keio University

Dr. JIMBO Ken Senior Research Fellow, the Japan Forum on International Relations (JFIR)

### <Korea>

Prof. Jae Ho CHUNG Professor and Chair, Department of International Relations, College of Social Sciences, Seoul National University

### <Malaysia>

Dato' Mohamed JAWHAR Hassan Chairman and CEO, Institute of Strategic and International Studies Malaysia

### <Singapore>

Mr. Simon TAY Chairman, Singapore Institute of International Affairs

### <Thailand>

Dr. Prapat THEPCHATREE Chair, ASEAN Studies Program, Institute of East Asian Studies, Thammasat University

### <USA>

Mr. Ralph COSSA President, the Pacific Forum CSIS

Dr. Charles MORRISON President, the East-West Center

### <CEAC>

Prof. ITO Kenichi President, CEAC

Prof/Amb. ISHIGAKI Yasuji Vice President, CEAC

### <GFJ>

Amb. KAI Noritake Governor, the Global Forum of Japan (GFJ)

*In Alphabetical Order*

## 8. (3) Curriculum Vitae of Participants

### <Indonesia>

**Dr. Edy PRASETYONO**      **Head of Department of International Relations, Centre for Strategic and International Studies (CSIS)**

B.A. from University of Indonesia in 1989, and MA and Ph.D. from Birmingham University in 1999 and 2001, respectively. Served as a visiting fellow, Japan Institute of International Affairs (JIIA) (1991), a visiting researcher, Australian Defense Studies Center (1993), and a visiting lecturer, Air Force Staff College (1992-1997). Concurrently, serving as a member of the Indonesian Committee, Council for Security Cooperation in Asia Pacific (CSCAP), a visiting lecturer at the Naval Staff College, Indonesia, and visiting lecturer of Joint Staff College Indonesia. His research interests include security issues in Asia Pacific, defense and military studies.

### <Japan>

**Prof. TANAKA Akihiko**      **Professor, the University of Tokyo**

B.A. from the University of Tokyo, Ph.D. from Massachusetts Institute of Technology. Served in various positions including Visiting Professor, Rhur-Universitaet (1986-87), Senior Associate Member, St Antony's College, Oxford (1994-95), Member, Asia-Europe Vision Group (1998-99), Member, East Asia Vision Group (1999-2001), Member, Initiative toward Japan-ASEAN Comprehensive Economic Partnership Discussion Group (advisory group for Chief Cabinet Secretary) in 2002. His research includes theories of world politics, contemporary international relations in East Asia, and issues in Japan-U.S. relations.

**Prof. AOKI Tamotsu**      **Professor, Waseda University**

B.A. and M.A. from the University of Tokyo, and Ph.D. from Osaka University. Served as Professor, Osaka University, the University of Tokyo, and National Graduate Institute for Policy Studies, and Chairperson of the Prime Minister's Committee on the Promotion of Cultural Diplomacy of Japan. Received the Medal of Purple Color from the Government of Japan in 2000. Concurrently, serving as Chairperson of Cultural Policy Committee of Cultural Agency, Ministry of Education, Science and Sports.

**Dr. FUKUSHIMA Akiko**      **Senior Fellow and Director of Policy Studies, National Institute for Research Advancement (NIRA)**

M.A. from the School of Advanced International Studies at Johns Hopkins University and Ph.D. from Osaka University. Served as Adjunct Professor, Keio University (2000-02), Visiting Professor, University of British Columbia (2002-03), and Visiting Professor, Kuwait University in 2005. Served as members for numerous committees of the Japanese government including the Defense Strategy Study Group and the Defense Agency's Council on Defense Facilities.

**Prof. URATA Shujiro**      **Professor, Waseda University**

B.A. from Keio University in 1973, and M.A. and Ph.D. from Stanford University in 1976 and 1978 respectively. His specialized fields include International Economics and Development Economics. Served as Director General, Research Institute, People's Finance Corporation (1997-99) and Professor, Waseda University, School of Social Sciences (1994-2005), and currently Professor, Graduate School of Asia-Pacific Studies. Concurrently serves as Research Fellow, Japan Center for Economic Research, and Faculty Fellow, Research Institute of Economy, Trade and Industry.

**Prof. SHIRAI Sayuri**      **Professor, Keio University**

M.A. from Keio University in 1989. M.Phil. and Ph.D. in Economics from Columbia University in 1991 and 1993 respectively. Her research interests include international finance, finance/capital market development, fiscal decentralization in Japan, and the Asian economy including India. Served in the International Monetary Fund as an economist (1993-98) and the Asian Development Bank Institute (2000-03) as a visiting scholar. Concurrently a member of various governmental advisory and research committees including those in the Ministry of Finance, Cabinet Office, and Ministry of Economy, Trade and Industry.

**Dr. JIMBO Ken**                    **Senior Research Fellow, the Japan Forum on International Relations (JFIR) and Associate Professor, Keio University**

Ph.D. from Keio University in 2005. Served as Research Fellow, the Japan Institute of International Affairs (JIIA) (1999-2003), Director of Research, the Japan Forum on International Relations (JFIR) (2003-04), and Executive Secretary at the Council on East Asian Community (CEAC). His research interests include Japan-US Security Relations, Multilateral Security in Asia-Pacific, and Regionalism in East Asia. Also serves as a foreign policy advisor at the Foreign Affairs Division, Policy Research Council at Liberal Democratic Party (LDP) and as an adjunct consultant on foreign policy at Democratic Party of Japan (DPJ).

<Korea>

**Prof. Jae Ho CHUNG**                    **Department of International Relations, College of Social Sciences, Seoul National University**

Ph.D. from the University of Michigan in 1993. Served as Visiting Senior Fellow, East Asian Institute, National University of Singapore (2004) and NAPS Fellow, The Brookings Institution (2002–2003). Concurrently, serves various positions including Advisory Council Member, Ministry of Unification, Advisory Council Member, National Security Council and KIDA-Fellow, Korean Institute for Defense Analysis. He is the Founding Coordinator of the Korean Association of Chinese Political Studies (KACPS). Specializing in Chinese politics, especially center-province relations and Sino-Korean relations.

<Malaysia>

**Dato' Mohamed JAWHAR Hassan**                    **Chairman and CEO, Institute of Strategic and International Studies Malaysia**

Served in various positions in the government including Director-General, Department of National Unity, Under-Secretary, Ministry of Home Affairs, Director (Analysis) Research Division, Prime Minister's Department, Principal Assistant Secretary, National Security Council, and Executive Secretary, Border Security Committee Malaysia/Thailand. Concurrently Member, National Unity Advisory Panel, Member, Penang State K-ICT Council, and Secretariat Council for Security Cooperation in Asia Pacific.

<Singapore>

**Mr. Simon TAY**                    **Chairman, Singapore Institute of International Affairs**

LL.B Hons. from National University of Singapore, LL.M from Harvard University, and Fulbright Scholar at Harvard Law School (1993-94). Served in various positions including Adviser to the Singapore delegation to the WTO Ministerial meeting in 1999, Senior Member of the Singapore delegation in the World Summit on Sustainable Development in 2002, and Nominated Member of the Singapore Parliament (1997-2001). Currently serves on a number of international and regional expert and eminent person panels, including the ASEAN Regional Forum register of eminent persons and experts, the APEC peer review process on trade, and the Eminent Persons Group on the ASEAN-Japan Centre.

<Thailand>

**Dr. Prapat THEPCHATREE**                    **Chair, ASEAN Studies Program, Institute of East Asian Studies, Thammasat University**

B.A. in Political Science (International Affairs) from Thammasat University; M.A. in Political Science (International Relations) from Ohio University; Ph.D. in Political Science (International Relations) from University of Georgia. Served positions such as Counsellor, Division 4, East Asian Department, MFA; Director of Center for International Policy Studies (CIPS), and Associate Dean for Research and Development, Faculty of Political Science, Thammasat University. His research interests are ASEAN, Thai Foreign Policy, Foreign Policy Analysis, International Security, and International Political Economy. Also the Vice President of the Association for American Studies in Thailand.

<USA>

**Mr. Ralph COSSA      President, Pacific Forum CSIS**

Served in the United States Air Force (1966-93), achieving the rank of Colonel, and last serving as Special Assistant to the Commander-in-Chief, U.S. Pacific Command. Served previously as Deputy Director for Strategic Studies, the National Defense University's Institute for National Strategic Studies. Concurrently Board Member of the Council on U.S.-Korean Security Studies and the National Committee on U.S.-China Relations (NY), Member of the International Institute for Strategic Studies (London) and the Asia Foundation's Task Force on America's Role in Asia. Also, Member of the ASEAN Regional Forum (ARF) Experts and Eminent Persons Group and Founding Member of the Steering Committee of the multinational Council for Security Cooperation in the Asia Pacific (CSCAP).

**Dr. Charles MORRISON      President, the East-West Center**

Ph.D. in international relations from Johns Hopkins School of Advanced International Studies. Serving as an international chair of the Pacific Economic Cooperation Council (PECC). Founding member of the U.S. Asia Pacific Council, the U.S. National Committee for Pacific Economic Cooperation and a member of the U.S. Committee for Security Cooperation in Asia Pacific. Served as a chair of the U.S. National Consortium of APEC Study Centers, a director of the Center's Program on International Economics and Politics and a former U.S. Senate aide and a research adviser to binational Japan-U.S. commissions. He specializes in issues on Asia Pacific international relations U.S. Asia policy and trade policy.

<CEAC>

**Prof. ITO Kenichi      President, CEAC**

Graduated from Hitotsubashi University and studied at Harvard University. Entered Japanese Foreign Service in 1960 and served various positions, including embassies in Moscow, Manila, Washington and Director of First Southeast Asian Division until 1977. Since then until 2006 he was a professor of international politics at Aoyama-Gakuin University. He concurrently serves as a founding president of the Japan Forum on International Relations (JFIR), the Global Forum of Japan (GFJ) and the Council on East Asian Community(CEAC). He is also a professor emeritus of Aoyama- Gakuin University.

**Prof/Amb. ISHIGAKI Yasuji      Vice President, CEAC**

B.A. in Law from Tohoku University and B.A. in Government from Oberlin College, U.S. Entered the Ministry of Foreign Affairs in 1959 and served various positions including Director, Southwest Asia Division, Deputy Director-General, U.N. Bureau, Amb. to the Dominican Republic and Jamaica (1992-94), Lebanon (1994-97), and Finland and Estonia (1998-2000). Concurrently serves as Professor, Tokai University Law School (International Law) and Councilor, the Japan Forum on International Relations. Current position since 2005.

<GFJ>

**Amb. KAI Noritake      Governor, GFJ**

Graduated from Hitotsubashi University. Entered the Ministry of Foreign Affairs in 1964. Served various positions including Director of the First Africa Division, Deputy Chief of Protocol, Ambassador to Panama, Ambassador to Lebanon, Ambassador to Tunisia, Professor at Kagoshima Prefectural College in 2003. Concurrently, Executive Director of the Japan Forum on International Relations.

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